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ABSTRACT

This final report of the Nebraska School Financing Review Commission includes the following items: (1) an examination of the role of income as a revenue source and indicator of wealth; (2) investigation of ways to reduce reliance on property tax for school support; and (3) consideration of alternate state aid distribution formulas. Also included are a list of statutes, historical overview, description of the current school finance structure, and review of court decisions. Findings support the implementation of a plan that includes: dedication of state income tax revenues to educational funding; increasing levels of state aid; limitations on school district budgets; development of a new equalization formula based on student needs and measurement of district wealth in terms of income and property tax resources; and provision for ongoing state revenue sources. Appendices contain an outline of state aid legislation history and statistical tables. Six figures and 16 tables accompany the text. (LMI)

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FUNDING NEBRASKA'S SCHOOLS: Toward a More Rational and Equitable School Finance System for the 1990s

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FINAL REPORT OF THE:

Nebraska School Financing Review Commission to the Nebraska State Legislature

January 1, 1990

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FUNDING NEBRASKA'S SCHOOLS: Toward a More Rational and Equitable School Finance System for the 1990s

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Nebraska School Financing Review Commission
to the
Nebraska State Legislature

January 1, 1990

Nebraska State Legislature

719 Donegal
Papillion, Nebraska 68046

Legislative Address:
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SENATOR RON WITHEM
District No. 14

January 1, 1990

The Honorable William Barrett
Speaker of the Legislature
District 39
State Capitol
Lincoln, NE 68509

Dear Senator Barrett:

On behalf of the Commission, I am honored to present to you the Final Report of the Nebraska School Financing Review Commission. The Report is the culmination of over eighteen months of steadfast work by the Commission. The Commission, through its numerous public meetings and public hearings, as well as innumerable hours of informal discussions by members and staff, has striven to reach consensus on a school finance plan which could resolve the major problems in school finance in a way acceptable and supportable by Nebraskans of all persuasions.

The Report focuses on the closely connected problems of excessive reliance on the property tax for support of our schools and the disparities in school districts' abilities to provide equitable educational opportunities for all of our students. Resolution of these problems are critical, not only in the interest of sound and fair tax and education policy, but in the interest of future growth and development of Nebraska's citizens and the state's economic well-being.

The Report supports implementation of a plan which will broaden the tax support for our schools through dedication of income tax revenues for schools and increased levels of state aid. A new equalization formula sensitive to current school district needs and income wealth in addition to property wealth is also proposed. To insure a tax shift away from the over-burdened property tax to alternate tax sources, limitations on school district budget growth are included in our plan. The plan recognizes the need for enhanced state revenue sources to insure ongoing and stabilized funding for our schools.

The education of our youth is the key to Nebraska's future. The Commission presents this plan to the Legislature for its consideration, as required by LB 940 (1988) and LB 312 (1989) in the hope that state policy makers will seriously consider it in light of the Legislature's obligation to provide appropriate education for our children in the public school system of our state.

Sincerely,

Ron Withem

Senator Ron Withem, Chair
Committee on Education

COMMITTEES

- Chairperson, Education
- Education Commission of the States
- Committee on Committees
- Government, Military and Veterans Affairs
- Rules
- Legislative Council

ACKNOWLEDGEMENTS

The work of the School Finance Review Commission and the preparation of this final report would have been impossible without the contributions and able assistance of a large group of people. We wish to acknowledge all who played a role and offer our gratitude.

First, the Commission benefitted from presentations by professionals in the Department of Revenue, including Dennis Donner, Mark Beck, Mike Gomez and Tax Commissioner John Boehm. From the Legislature's Revenue Committee, valuable assistance came from George Kilpatrick, Eric Will and Kendra Kluge. From the Legislature, early staff assistance was provided by Corey Phillips, Legislative Aide to Senator Roger Wehrbein and Dawn Egenberger Rockey, former Legislative Aide to Senator Jerry Miller and current Administrative Assistant to Senator Ron Withem. From the Governor's Policy Research Office, we recognize the contributions of Andrew Cunningham.

The Commission wishes to specially recognize and thank a core group of staff who were instrumental in support of the Commission. These include: Larry Scherer, Legal Counsel to the Education Committee who served as staff coordinator; Tim Kemper from Management Information Services in the State Department of Education, the Commission's number cruncher, logician and conscience; Sandy Myers from the Legislative Fiscal Office; Bill Lock and Dick Hargesheimer from the Legislative Research Division; Kim Davis, Legislative Aide to Senator Dennis Baack; Tim Erickson, Legislative Aide to Senator Scott Moore; Marcelle Williams, Research Division of the Nebraska Department of Revenue; and Russ Inbody from the Finance Division of the State Department of Education. The hours of time and talent committed by all of these individuals, in addition to their regular duties, should not go unnoticed.

The Commission was fortunate to benefit from the advice and counsel and analysis of consultant Dr. John Augenblick, of AVA, Inc. in Denver. Dr. Augenblick helped the Commission to examine its plans and goals, under the microscope of commonly accepted school finance principles and measures of school finance equity. In addition, the Commission benefitted greatly by the presentations of Dr. Dale Dennis of the Kansas Department of Education and Charles Brown, Director of the Colorado Legislature's Legislative Services Division.

The Commission would like to provide special recognition to LaRue Wunderlich, the Committee Clerk of the Legislature's Education Committee, who provided able clerical and support services to the Commission, including typing of the Commission's interim report and the draft of its final report. The Commission, finally, would recognize and thank Linda Soto, Administrative Assistant at the Legislative Research Division for her services in typing and formatting of the Final Report.

Although it is somewhat unusual, the Commission would also like to thank and express its sincere appreciation to one of its members, Dr. Larry Vontz who is the Deputy Commissioner for the State Department of Education. Without Dr. Vontz's unique ability to translate complex concepts into laymen's terms the Commission would have been forced to spend a great deal of extra time in study. Dr. Vontz truly served as the Commission's school finance "teacher" in the highest and best sense of that term.

On behalf of the Commission,

Senator Ron Withem, Chair
Committee on Education

EXECUTIVE SUMMARY

The Nebraska School Finance Review Commission was created by the Legislature in LB 940 (1988) to make an in-depth and objective review of the funding of Nebraska's public school system. The Commission was charged with the examination of whether or not income as a revenue source and indicator of wealth should play a larger role in school finance. It was also to look at methods to reduce the burden on the property tax for school support and consider state aid distribution formulas which provide greater equity for Nebraska students and taxpayers.

The Commission was composed of representatives appointed by the Governor from all classes and sizes of school districts, members of the public at large, representatives of higher education, a representative of the Governor, a representative of the Commissioner of Education and members of the Legislature. This diverse group of individuals united to work on the complex and often emotional issue of school finance in a cooperative and positive spirit. The Commission held over twenty public meetings, five public hearings and listened to innumerable presentations of staff and outside experts, in order to reach its conclusions on how Nebraska might implement a school finance system which is fairer for Nebraska taxpayers and students.

The Commission found two major problems with the way Nebraska currently funds its public school system. First, the burden on property for school support is excessive by any standard of measurement, resulting in inequities to taxpayers and a narrow and unstable tax base for schools. Second, the current system of school finance, with its overemphasis on the property tax as the primary basis of support for schools and grossly inadequate

equalization abilities, does not assure that all students in the state will have equitable access to appropriate and necessary school services.

Further, the Commission found that the historic resistance to greater equalization of school fiscal support in Nebraska was closely related to the inability of Nebraska policy makers to reach consensus on what constitutes "wealth" in terms of school district resources and in terms of taxpayers' ability to pay for educational services. The Commission felt that removal of this perennial rural-urban stumbling block was critical in order for there to be widespread public support for a greater state role in school funding. It concluded that the utilization of income tax revenues as a dedicated revenue source for schools and as an indicator of school district wealth was a necessary and crucial factor for an improved school funding system.

The Commission also concluded that some form of limitation on school district budget growth would be an essential and necessary component of a plan for school finance which entailed a substantial tax shift in the means by which Nebraska supports its public schools. In order to convince Nebraskans and their political leaders of the wisdom and necessity for greater state tax support for schools and a corresponding lessening of property tax support for schools, the Commission became convinced that real and effective budget limitations are a political necessity. Only budget limits will guarantee a real shift in the burden of tax support for Nebraska public schools.

The Commission also recognized early that a decrease in property tax support for the schools could be effectuated only through corresponding increases in state tax support for schools. The Commission found that it would be unrealistic and damaging to public education in this state to expect significant decreases in school spending as a means of property tax relief because Nebraska schools spend below or near average on both a per pupil and per capita basis. Increases in state taxes are the political cost which Nebraskans must be willing to pay in order to reap the benefits of short-term and long-term property tax relief and educational equity.

The Commission believed that any system of school finance should be guided by a few overriding principles and beliefs about the purpose of state involvement in the financial support of the school system. In other words, it was crucial to understand why Nebraska provides state aid to schools in order to make decisions about the kind of state aid program which will benefit Nebraska. The Commission came to believe that the purposes of state aid are:

1. First, to assure all Nebraska children an equitable opportunity for an appropriate education;
2. Second, to provide a broad and stable system of financial support for public schools through an appropriate mixture of revenue sources; and
3. Third, to provide equalization of fiscal ability and financial support among school districts and taxpayers through a distribution formula which recognizes school district needs and school district wealth.

Further, the Commission believes that "wealth" as it relates to school districts' ability to provide educational services and in terms of taxpayers' ability to pay for such services, must include consideration of income tax revenues as well as property tax revenues.

With due regard for these findings and beliefs the Commission has proposed the following recommendations for a new school finance system:

1. **Twenty percent of all state income tax revenues should be dedicated for public school support. Twenty percent of all individual income tax proceeds which are attributable to specific school district should be returned directly to the school district where such income tax revenues originated.**

   This recommendation will assure a broadened, growing and more stable base of support for all public schools.

2. **There should be an increase in the overall level of state support to a target level of 45 percent of the aggregate operational costs of the school system in order to effectuate a 15 percent reduction in aggregate property taxes which will be levied (or a 20 percent reduction in aggregate property taxes to be levied for support of the schools).**

   This recommendation will assure a meaningful and realistic reduction, over the short and long term, in the share of school costs which must be supported by the property tax.

3. **The Legislature should implement an equalization based distribution formula which will assure that all school districts have the fiscal ability to provide for the realistic needs of students and which will measure school district wealth in terms of both its available income tax resources and property tax resources.**

   This recommendation will help assure that the state is meeting its responsibilities to provide equitable educational opportunities for students and fair tax treatment of its citizens.

4. **In conjunction with increased state support for the schools, there should be an implementation of real and effective growth limitations on the budgets of public schools. These limitations should be sensitive to differences in needs and resources of the schools.**

   Budget growth limitations will assure that the increase in state support does result in reduced property tax support for schools. For the initial year of implementation, the Commission is recommending a budget growth range of 4 percent to 6.5 percent.

5. **The Commission recommends that its proposed school finance plan should be funded on an ongoing and sustainable basis from appropriate increases in the state sales and/or income taxes as determined necessary and appropriate by the Legislature.**

   The Commission recognized its duty to suggest a tax source or sources which will be necessary to implement its plan. It did not feel it appropriate to propose specific revenue increases since this will be a function of the Legislature and the Governor in light of constitutional duties to set a budget based on projected revenues and total budget obligations.

This is a plan for a new school finance system which the School Finance Review Commission submits to the Legislature in fulfillment of its statutory obligations under LB 940. The Commission recommends that the Legislature and Governor give this plan serious consideration in the 1990 session of the Unicameral.

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STATUTES LB 940 (1988) AND LB 312 (1989)

79-1378

The School Financing Review Commission is hereby created. The commission shall consist of sixteen members, including: (1) Three members of the Legislature; (2) two individuals from higher education with expertise in the area of school finance; (3) the Commissioner of Education or his or her designee; (4) a representative of the Governor; (5) a member residing in a Class I school district; (6) a member residing in a Class II school district; (7) two members, each residing in a Class III school district; (8) a member residing in a Class IV school district; (9) a member residing in a Class V school district; (10) a member residing in a Class VI school district; and (11) two members from the state at large.

The members described in subdivisions (1), (2), and (4) through (11) of this section shall be appointed by the Governor with the approval of the Legislature within thirty days after July 9, 1988, to serve through June 30, 1990. Vacancies shall be filled by the Governor for the remainder of the term. No member of the commission shall receive any compensation for his or her services. Reimbursement shall be provided for reasonable and necessary expenses incurred by members of the commission as provided in sections 81-1174 to 81-1177.

The commission shall cease to exist June 30, 1990.

79-1379

The School Financing Review Commission shall conduct an indepth review of the financing of the public elementary and secondary schools. The committee shall:

1. Examine the option of using income as a component in the financing of schools;
2. Examine financing methods used in other states which offer alternatives to the current heavy reliance on property tax;
3. Examine financing issues as they relate to the quality and performance of the schools;
4. Prepare a report with recommendations and a plan to implement the recommendations. An interim report shall be presented to the Legislature by March 1, 1989. A final report shall be presented to the Legislature by January 1, 1990; and
5. Establish or recommend the creation of an oversight committee to aid in the implementation of the plan pursuant to subdivision (4) of this section and necessary adjustments to legislation enacting such plan.

79-1380

The School Financing Review Commission shall have the power in carrying out its duties:

1. To hire staff including consultants;
2. To obtain assistance from the State Department of Education and the Department of Revenue in acquiring data needed to carry out its duties; and
3. To contract for any necessary facilities, equipment, and services including computer services.

79-1381

The Legislature shall appropriate from the General Fund such money as may be necessary to permit the School Financing Review Commission to carry out its duties. The appropriation shall be at least one hundred thousand dollars.

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INTRODUCTION

A Bit Of History

School finance has been an issue for the State of Nebraska since before Nebraska became a state. The territorial Legislature authorized the creation of school districts to provide primary and secondary education and required each school district to levy 2 mills for support of the schools. The state matched this with its own 2 mill, statewide levy for schools (primarily teachers salaries) for inhabitants of the territory. Thus, in the 1860s, school finance became an issue. (See Appendix A for a historical outline of school finance legislation.)

Education has always been a legal responsibility of the states. States were required as one of the conditions for entry into the union to establish common public schools for the children of the state. Nebraska recognizes this responsibility through the language of Article VII, Section 1 of the State Constitution which reads "The Legislature shall provide for the free instruction in the common schools of this state for all persons between the ages of five and twenty-one years." As noted above, this responsibility was delegated to school districts. In recognition of its constitutional duty, the Legislature has explicitly stated its goal and mission for the public school system in section 79-4,140.01 R.R.S. 1943 (1987). The primary source of funding for the schools has always been local property taxes, although the state for many years did provide for a uniform state levy for schools. Since the adoption of the "Duis Amendment" to the Nebraska Constitution, Article VIII, Section 1A, 1966, the state may not levy a property tax for state purposes. Thus, property

taxation for public schools is a local authority delegated to all schools. There is no statutory limit on this levy authority for operational general fund support of the schools.

Other than the financial support from the school lands and trust funds, a relatively small amount in the context of total costs, the Nebraska Constitution does not mandate any specific form of financial support. Historically, Nebraska has evolved as a strong local control state and school finance has been closely tied to the local property tax authority which was granted to schools early in our history as a state.

As will be discussed in more detail in the following section, the Legislature came into the modern era of "state aid" as a source for school funding in 1967 with the adoption of the current Foundation and Equalization Act. This legislation was made possible by adoption of constitutional amendments allowing state sales and income tax systems in the 1960's. According to Senator Jerome Warner, the primary sponsor of LB 448, the purposes of the Foundation and Equalization Act were: "First, it is a means of lowering property tax at the local level; secondly, to equalize the costs between the school districts; third, to provide equal educational opportunities for all the children in the state. We have to recognize that the ability to pay for education is directly related to the type of education that can be provided within a school district and that under the property tax system, children and accessible wealth may or may not be located within the same school district. And fourth, to me school organization in the state cannot properly be gone forward with under the present tax structure. We cannot expect many of our rural areas particularly to incorporate themselves with ....urban areas for school purposes when the property tax provides better than 80 some percent of the local support for local education." Education Committee hearing on LB 448, 1967.

The Commission believes that the original Foundation and Equalization Act, with its heavier emphasis on funding for equalization in the early years, was a reasonable and workable approach to school finance. Unfortunately, the Legislature has not maintained the funding of the act and, as will be pointed out in the following sections, the current act's

definition of needs and wealth have not been updated to reflect substantial changes in these areas in the past 22 years.

While this current law has been tinkered with many times over the past 22 years, the basic provisions of the Foundation and Equalization Act remain unchanged. However, the funding provided through state aid has never provided a major portion of the costs of operating the public schools. A more detailed description of the current finance formula may be found in Appendix B of this report and a later section of this report, "The Current School Finance Structure".

Legislative Bill 940

Legislative Bill 940, which created the School Finance Commission, was enacted in 1988, and arose out of a study on school reorganization by a group called the Ad Hoc Committee on Public School Policy. The Ad Hoc Committee was impaneled by the Governor and Chair of the Education Committee in 1987 in an attempt to find some accommodation on the perennially difficult issue of school reorganization. The Ad Hoc Committee believed it could not address the school reorganization issue in isolation from school finance and quality. Subcommittees on school finance and accreditation were created to address these issues in greater detail.

For years rural interests had argued the unfairness of the current equalization formula which measured school district wealth and taxpayer ability to finance school costs solely on the basis of property wealth in the district. Because agriculture is, by its nature, a capital intensive industry, it was argued that the ability of taxpayers to support schools should not be necessarily dependent on the value of property owned. Urban forces countered that property valuation and property taxes are the only form of wealth to which schools have access and over which they have control.

The finance subcommittee recommended to the full Ad Hoc Committee that Nebraska adopt a finance system similar to Kansas' system. The subcommittee was especially

interested in the way in which Kansas had integrated income into the Kansas finance system. Members were convinced that inclusion of income as a revenue source for schools and as a determinant of school district wealth would help resolve the perennial dispute between rural and urban legislators and educators over the proper definition of school district wealth. As will be discussed later in the Commission's Findings, the Commission agreed that inclusion of income as a component of school district wealth is a valid and important proposition.

Like the introducer of the current state aid plan in 1967, the finance subcommittee was also convinced that the current heavy reliance on property taxes and the great disparity in tax levies which exist in the state presented a deterrent to school reorganization based on the education interests of children. Therefore, the other major charge of the School Finance Review Commission would be to investigate finance systems which do not place as much reliance on the property tax for school support.

Finally, the Ad Hoc Committee felt the study should include a look at whether performance and quality should be factored into school finance formulas. The Ad Hoc Committee's concern with accreditation and quality factors was the source of this portion of the School Finance Review Commission's charge.

Study Processes

The School Finance Review Commission was appointed in August of 1988 and held its first meeting on August 31, beginning its discussion of school finance philosophy. Over the course of some 18 months and a total of 21 meetings, the Commission has striven to reach a consensus on the important goals and objectives of providing state aid to schools.

Early on, the Commission reaffirmed the traditional goals of state aid: (1) Providing a broad and stable support base for education with a shift away from excessive property tax support and (2) reducing inequities in school districts' ability to provide educational

opportunities for children. These dual goals have underpinned nearly all of the Commission's work.

A thorough immersion in the statistical context for school finance in Nebraska was provided to the Commission at its first meeting. Data on state aid distributions, number of districts and enrollment, financial data on receipts, revenues, valuation, levies, cost indexes, and average costs were presented to the Commission and are to be contained in the School Finance Review Commission supplementary information volume.1

In subsequent meetings, the Commission heard presentations describing our current school finance formula. Dr. Dale Dennis of the Kansas State Department of Education presented the Commission with a thorough explanation of the Kansas system and Charles Brown of the Colorado Legislative Research Department gave a similar presentation on Colorado's new formula. The Commission also heard reports on the finance formula proposed by the Nebraska Council of School Administrators (NCSA) in 1985 and 1986. Several of the items in the Commission's proposed plan were borrowed from the NCSA plan and the Kansas model. The Commission was made aware of the numerous attempts at property tax relief and school finance reform which have failed in the past, including prior efforts to institute local option income taxes for school support.

The Commission was made cognizant of the past and current narrowing of the property tax base through exemptions, both statutory and court mandated. It further was made aware of assessment issues and problems by means of presentations by the Nebraska Department of Revenue.

The Commission met with members of the legislative committee guiding the Comprehensive Tax Study completed by Syracuse University. Discussion centered on the tax study's recommendation that mandatory reorganization should occur prior to any significant state effort to reform its school finance system. As noted below, the Commission rejected this idea.

The Commission, during the 1988 Legislative Session, was aware of the "property tax relief" legislation which was being debated. The Commission took the position, eventually embodied in LB 611 and LR 189, that the "pure" property tax relief proposals, such as LB 84, were interim answers to the property tax problem while adoption of a major school finance reform package was the appropriate long term solution.

In March, the Commission presented its interim report to the Legislature stating the following goals:

1. A 15 percent reduction in aggregate property taxes levied and a 20 percent reduction in aggregate property taxes levied in support of the schools;
2. Increased level of state support to approximately 45 percent;
3. A rebate of 20 percent of individual income taxes to the district where such taxes are generated in addition to revenue added from increased state sales or other taxes;
4. A limitation in growth of school budgets;
5. Consideration of a sales tax increase or other revenue enhancements to fund the plan.

The interim report also supported the concept of an equalization formula similar to that used in Kansas to insure that necessary financial resources are available for each child in the state and that all children have a more equitable opportunity for an appropriate education with consideration given to vast geographic and financial disparities of Nebraska schools.

During June and July of 1989, the Commission took this interim package to the public through a series of five public hearings. This plan was also aired at four public hearings held jointly by the Legislature's Revenue and Education Committees pursuant to LR 189. There was substantial agreement on the shift away from the property tax for support of the public schools and broadening of the tax base with the income tax rebate concept. Educators and members of the public had an opportunity to become familiar with the philosophy and mechanics underlying the new formula.

While there are many reservations and some opposition to the proposed budget limitations, educators indicated some recognition that a tax shift in support of schools was not likely absent some guarantees of property tax relief through budget growth limitations.

The Commission's plan was revised following the public hearing phase. Changes modified the enrollment tier structure and provisions of the budget limitation. After several additional meetings, the Commission resolved many difficult issues and reached some agreement on the plan for school finance in Nebraska for the 1990s and beyond.

Prior to a description of the funding and final recommendation of the Commission, it will be useful to paint a picture of the current school finance system and note some of its deficiencies. This may be found in the section entitled "The Current School Finance Organizational Structure." A later section, "School Finance in the Courts", is presented to provide information on how the Commission was influenced to a certain degree by the threat of litigation challenging the state's school finance system. Recent court decisions in Montana, Kentucky and Texas are discussed. Those cases overturned the school finance systems in those states. Dr. John Augenblick's presentation to the legislative issues symposium provides a summary of the current national legal situation nationwide. A lawsuit challenging the Nebraska school finance system was filed in Lancaster County on January of 1990.

THE CURRENT SCHOOL FINANCE STRUCTURE

For Nebraska's 838 school districts and approximately 64 county nonresident high school tuition funds, financial support comes from a variety of sources. The primary source of funding for public schools is from property taxes, with total local sources comprising 66.46 percent of the funding to local school districts for 1987-88. The second largest source of funds comes from the Foundation and Equalization Fund, Nebraska's form of general state aid for schools. Total state funding consists of 22.96 percent of all revenues to local school districts, while federal support amounts to 6.69 percent, and non-revenue receipts account for 3.89 percent. (Page 3 of Appendix C is a compilation of these sources and their dollar amounts taken from the 1987-88 school finance reports.)

The Foundation and Equalization Program, enacted in LB 448 in 1967, is composed of three major components: Foundation Aid, Incentive Aid, and Equalization. Pages 1-3 of Appendix B describe the three components and lists the corresponding dollar amounts that were distributed for the 1989-90 school year. A total of $133,616,100 or approximately 13 percent of total revenue sources to local schools was distributed through this formula for 1989-90. Page 5 of Appendix B shows the history of legislative appropriations to the Foundation and Equalization Program, beginning with the 1968-69 school year through the present school year 1988-89.

The foundation program accounts for the largest portion of the appropriation, amounting to $96.4 million of the total $133.6 million for the 1989-90 school year. All school districts receive foundation aid, which can be defined as a flat grant per pupil in resident enrollment weighted to reflect the varying costs of educating students at different grade levels. A

school district's needs or property wealth are not taken into account when distributing foundation aid.

School districts with high needs and low property wealth qualify for equalization aid, since equalization is sensitive to both factors, but only to a limited degree. Page 2 of Appendix B shows that the state only guarantees a need factor for grades 9-12 of $1,479.79 per student for state aid payments in 1989-90, whereas the typical cost for a high school student is usually three times that amount. The reason for the wide variance in the amount that is guaranteed per student and the actual cost per student is because the need level of the current equalization formula is dependent on available state appropriations, not actual costs. Also, the minimum qualifying levy of 42 cents per 100 dollars of value for K-12 districts and lesser prorated levies for Class I and Class VI districts reflects only about one-third or one-fourth of typical actual levies. These limitations seriously reduce the ability of the current equalization formula to assure that districts have the resources available to provide an appropriate educational program for all students.

Nebraska school districts are divided into six statutory classifications (Class I through Class VI) and are described as follows:

1. Class I shall include any school district that maintains only elementary grades under the direction of a single school board;
2. Class II shall include any school district embracing territory having a population of one thousand inhabitants or less that maintains both elementary and high school grades under the direction of a single school board;
3. Class III shall include any school district embracing territory having a population of more than one thousand and less than one hundred thousand inhabitants that maintains both elementary and high school grades under the direction of a single board of education;
4. Class IV shall include any school district embracing territory having a population of one hundred thousand or more and less than two hundred thousand inhabitants that maintains both elementary and high school grades under the direction of a single board of education;
5. Class V shall include any school district embracing territory having a population of two hundred thousand or more that maintains both elementary grades and high school grades under the direction of a single board of education; and
6. Class VI shall include any school district in this state that maintains only a high school. (79-102 R.R.S.)

The Commission recognized various unique needs and problems that are associated with the different classifications of school districts. Class I districts have special needs, due to

the sparsity of population, isolation, limitations of valuations, shrinking enrollment and lack of economic growth. Parents may experience high transportation costs or additional residential expenses due to the distant location of the high school. Most of Class II district's problems stem from declining enrollment. Usually state aid is not a major revenue source and although residents pay high property taxes, most are not willing to close their schools. Generally, Class III districts are also losing enrollment, although several of the larger Class III districts are growing. Class III districts rely heavily on the residential property tax base and the loss of railroad valuations has had a negative impact on these districts.

The Lincoln Public School system, as the only Class IV district, has experienced significant enrollment growth, which is likely to be sustained. The Commission found that the major problems for LPS focused on the building of new facilities and facility rehabilitation and repair to accommodate the increase of students. The majority of LPS's budget is for personnel, although they do transport a significant number of students. The Omaha Public School District, as a Class V school district, is the largest urban district between Denver and Chicago. Student turnover is a problem for OPS, as is declining enrollment, due to competition with wealthier, growing suburban districts. Omaha Public Schools have special needs, due to the desegregation plan and a large number of at-risk students. Class VI districts are generally rural in nature, have widely varying valuation per student and agricultural land valuation changes have had a major impact on them.

Of the states' 891 school districts in 1987-88, 590 were Class I districts, of which 181 Class I districts were part of the 23 Class VI districts. Fifty-four school districts were classified as Class II districts and 222 as Class III districts. Lincoln Public Schools and Omaha Public Schools are classified as a Class IV district and Class V district, respectively. (Page 1 of Appendix C)

The vast majority of school districts are Class I districts with accompanying Class 6 and/or nonresident high school tuition funds. These districts account for only 9.01 percent of the resident enrollment and 14.44 percent of the valuation in 1987-88, out of a total K-12

resident enrollment of 265,606 and a total valuation of $44,239,460,392. Class II districts represent 2.85 percent of the resident enrollment and 3.97 percent of the valuation, compared with Class III districts which represent 63.04 percent of the resident enrollment and 55.92 percent of the valuation. The Lincoln Public School system contains 9.59 percent of resident enrollment and 10.27 percent of valuation, while the Omaha Public School System has 15.52 percent of the resident enrollment and 15.40 percent of the valuation in the state. (Page 1 of Appendix C)

Class III districts received $91,343,871.10 in Foundation Aid, Incentive Aid and Equalization Aid for the 1988-89 school year, or 68.4 percent of the total $133,616,100.07 appropriation. Class I districts received 5.3 percent, Class II districts 2.8 percent, the Class IV district 7.1 percent, the Class V district 13.5 percent, Class VI districts 1.6 percent and the county nonresident high school tuition funds received 1.3 percent of the state aid payments. (Page 4 of Appendix C)

Class II districts had the highest average general fund levy for the 1987-88 school year with 1.5205, while Class III districts levied an average 1.5081 per $100 of valuation. The Lincoln Public School system had a General fund levy of 1.3461, compared with the Omaha Public School system's levy of 1.4323. The average Class I district's levy of 1.2218 included both the elementary general fund levy and the nonresident high school tuition levy or the general fund levy of the Class VI district.

The Class I districts which educate only elementary students, have an average cost per student which is the lowest of all the classes of school districts at $2,963 per student for 1987-88. Class VI districts, which educate high school students only, have an average cost of $5,248.99 for the 1987-88 school year. Class II districts have an average cost per student of $4,889.53. Class III districts have an average cost per student of $3,447.12, with Omaha Public School's and Lincoln Public School's costs per student at $3,582.71 and $3,780.02, respectively. (Page 2 of Appendix C)

Nebraska's school districts are very diverse in size, needs and resources. Even within a class of school districts vary greatly.

SCHOOL FINANCE IN THE COURTS

Note: This section is an edited transcript of a presentation by Dr. John Augenblick, the Commission's consultant, to the Legislature at its annual Legislative Issues Symposium on November 13, 1989. Dr. Augenblick has served as a consultant to plaintiffs challenging state school finance systems and to states defending such systems or attempting to create new systems in the wake of court decisions declaring school finance laws to be unconstitutional.

I want to talk about the role of the courts in school financing. First, I want to review the history of the role of the courts in school financing. Second, I want to take the role of a plaintiff in one of these cases, and from that perspective talk about what it is that they're looking to show in these cases. Third, I'll take the role of a defendant, and talk about what the state has to do to defend itself. Finally, I'll summarize what it means when the courts get involved and end up declaring your system unconstitutional.

Since 1976, I've had a chance to watch the conduct of the courts in school finance through my role at ECS (Educational Commission of the States) as the director of their finance center. In addition, I have worked with plaintiffs in Colorado, Montana, New Hampshire and Texas. I'm currently working with people in Minnesota and North Dakota. I also have worked with several states after the court decisions came down, and that's a more difficult job. It's easier to take a side in these things and try and present your case. It's more difficult once the court has said something to actually correct the system. I've also had the dubious honor of working with Wyoming, Texas, and now with Kentucky, in trying to deal with these court decisions.

These are, in the words of a Chinese philosopher, interesting times, as far as this topic goes. If you had had me up here a year ago, there wouldn't have been much to talk about. We would have been talking about past history. But all of that has changed. As I looked

at these court cases between 1970 and 1983, which was when all the activity was going on around the country, there were seven states in which the Supreme Court declared the school finance system to be unconstitutional. Those states were California, the first, New Jersey, Connecticut, Washington, Wyoming, West Virginia, and the most recent of those was in Arkansas in 1983. Then, it's as if the court simply went to sleep between 1983 and the end of 1988; there wasn't a single case in which a system was declared unconstitutional. I figured the courts were out of it; states were taking these matters into their own hands, and the courts were no longer interested in this issue.

With the release of the National Education At-Risk report in 1983, attention shifted from the kind of issues that attracted the Court's attention to a whole different set of issues. For five years little happened in school finance. Suddenly things changed: In January 1989, Montana's system was declared unconstitutional; in June 1989, Kentucky's system was declared unconstitutional; and in October 1989, the Texas system was declared unconstitutional.

The question that you've go to ask yourself is, "Could this happen here--in Nebraska--and what would it mean if it did?" What I'm going to tell you is some of the story about why these things happen, and what happens when they happen. So, let's go back in time and talk about some of the first cases and why they came about.

You know that school finance is an important topic because it assumes a tremendous amount of your state budget. In most states, financing public schools accounts for 40-to-50 percent of the state's budget. If you add higher education, you can talk about two-thirds of the budget. So, this has been a topic that has been of concern for many years, yet the courts were not involved until the late 1960's.

At that time, in two states, Virginia and Illinois, plaintiffs representing school districts tried to demonstrate that the systems were unconstitutional for a very simple reason. The plaintiffs argued that the amount of money that the state was distributing to the schools was not related to the needs of those schools. It sounds like a very straightforward argument. They were saying that the state does not consider the various needs of school

districts when it allocates half of its general fund budget. The reason they brought these cases was to stimulate change in the way schools are funded.

At that time, most states still provided most state money through a flat grant. That is what they considered to be the most equitable way to do it. Rich and poor, large and small, everybody got the same amount per student or per classroom. States have wrestled with that idea for a long time, and they've come up with some other ways of doing it, but back in the 1960's state aid systems weren't very sensitive to the things that cause differences across districts. We know that size is a factor that affects the cost of delivering educational services. You may know that the proportion of kids who are in special education programs affects the cost of delivering a service. It may be that districts in one part of the state have a harder time paying for services than districts in another part, in sparsely populated districts with high transportation costs. You can create a laundry list, none of which most states really considered back in the late 1960's.

In both cases in the 1960's, in Virginia, and in Illinois, the courts threw the cases out. These cases were brought in federal court, not in a state court. The federal court said there is no standard by which to measure the needs of the districts. The plaintiffs may have been right in suggesting that states were not sensitive to the needs, but they were unable to demonstrate what those needs were and how they affected the cost of delivering service.

That was followed almost immediately by a case that's become the most famous one, the Serrano Case in California, That was the first of the cases that really changed the way we look at school finance. The plaintiffs in that case took a whole different tack. Rather than focusing on needs, and trying to measure them and account for them, which the accounting and measuring systems couldn't do, they took a different tack. They argued that education was a fundamental interest of the state. It was a fundamental right of children to receive an education in a state.

You need to start asking yourself, "Would any of these things apply in Nebraska?" If we went to court, would the court say that education in the state of Nebraska is a fundamental right, analogous to voting? In each of the ten states where their systems have

been declared unconstitutional, the court has said education is a fundamental right. But there are cases, such as in my own state, Colorado, where the court has thrown out the case. They said education was not a fundamental right. So it can go either way. You need to ask yourself, "What might they do here?"

The first leg that the Serrano Case stood on was proving that education is a fundamental right. The second leg was that the property wealth of school districts, which was the basis of a lot of their money, was a suspect classification. It was just as suspect as race, age, nationality, or any of the other things you've heard the U.S. Supreme Court talk about.

If these tests are met--if education is a fundamental right, and if property wealth is considered to be a suspect classification-- the courts will then apply a very strict test to whatever information is presented to it. The test they apply is referred to as the strict scrutiny test. That means they look very carefully at the data that they're presented, and the state (i.e., the defendant) has to demonstrate that there is a compelling reason for allocating money in the way that it is allocating it. The state can't simply argue "this is the way we've done it for years, this is rational, this makes sense, and it always has been so in our state." The court, if those conditions are met, will say, you must demonstrate a compelling interest in why you do it that way.

In California, the state was unable to demonstrate that. The court found the system unconstitutional. They found it unconstitutional under the U.S. Constitution's equal protection clause. They found it unconstitutional under the state's equal protection clause. They also found it unconstitutional, because it violated a goal. The goal was one that they called fiscal neutrality. Fiscal neutrality simply means that the education available to a child cannot be the function of the wealth of the district in which the child lives. It can only be a function of the wealth of the state as a whole. If it can be demonstrated that the wealth of the district in which the child lives influences the educational opportunities which are available to that child, that violates the principle of fiscal neutrality.

That approach was very powerful because it did not require the vast data collection that the Illinois and Virginia cases required. It required an entirely different way of looking at things. Suddenly lots of states picked up on that approach. Those of you who were around in 1973 might remember what was going on around the country. Plaintiffs were lining up cases. Legislatures were confronting the issue of whether they should change their school financing systems, for fear that this very simple approach could be applied in their state.

In 1973, a case very similar to Serrano was brought in Texas, and ultimately before the U.S. Supreme Court. The question was, "would the principles that apply in California also apply at the U.S. Supreme Court level?" The answer was that they did not. Meaning that there was not going to be a simple solution in which the U.S. Supreme Court said all school systems around the country were declared unconstitutional. The Court said that education was not a fundamental right guaranteed by the U.S. Constitution. Under the 10th Amendment, anything that is not explicitly granted to the federal government is referred back to the states. They said it because there isn't one word mentioned in the U.S. Constitution about education. In the federal constitution, unlike California's, education is not a fundamental right.

Second, in the 1973 Texas case, the court ruled that property wealth is not a suspect classification. Because of that, they discovered that wealthy people and poor people live in places that are designated as property poor, and wealthy people and poor people live in places that are designated as property rich. You could not necessarily use property wealth to be indicative of anything that would be analogous to race, or sex, and so on. People were too mixed up in poor districts and they were too mixed up in wealthy districts. So on both of those bases, they were able to say, we don't have to apply strict scrutiny. We only have to look at the Texas system and see whether or not it is rational. And the court was convinced that the state had established a rational system for allocating money to the school districts. They, therefore, let the system stand.

A month later, a case came down in New Jersey. In the New Jersey case, the judge did not rely on the United States Constitution. He relied on what is referred to as the "education clause" of New Jersey's Constitution. The education clause required that education services be available in a "thorough and efficient" way throughout the state of New Jersey. I come from New Jersey. I don't expect most of you would understand much about New Jersey, but you do know that it's not a very big place. Imagine a place that's one fifth the size of Nebraska. It has 600+ school districts in it. The variations in the spending, taxing, and wealth of those school districts is enormous. The court was able to use that "thorough and efficient" language to say that when you have that kind of variation you cannot possibly have a "thorough and efficient system". They were able to throw out that system.

Since New Jersey, school finance cases have all been in state courts. There has not been another attempt to deal with this in a federal court. Every case brings in the same issues that California brought in, the equal protection clause of the U.S. Constitution, of the state constitution, and the state education clause, which every state constitution has.

Every state constitution says something about education. For example, Connecticut, whose systems was found unconstitutional, uses the term "appropriate education" to be provided to every child in the state. The state court said that was not being done. In Washington, the state requires that "a basic and ample" education be provided to every student. The court was able to say that this was not being done. In West Virginia they use the words "thorough and efficient". In Texas, they use the words "suitable and efficient"; the court was able to say that those conditions were not being met. In addition, they have said that education is a fundamental right.

In the cases where plaintiffs have prevailed, the courts have said that you must look at the situation with what we have called strict scrutiny. On the other hand, in the cases that have not been successful from the plaintiff's perspective, the court has typically not looked at the system with strict scrutiny. A major point of contention is whether or not education

is considered to be a fundamental right. The second question is what exactly the education clause says, and how that will be interpreted by the court.

That is the history up to now, and the theory under which these cases are brought. What I wanted to go through with you is what it is that the plaintiffs are trying to show. As I go through this list, you'll want to think carefully about whether any of these things apply in this state. Because these are the kinds of things that plaintiffs will attempt to prove. Regardless of the theory in the case, these are the things that plaintiffs are looking for. When they find them, they know that the system will have a more difficult time defending itself.

We're (i.e., plaintiffs) going to try to find a tremendous amount of variation in the property wealth of the school districts. Now it's not very hard to find. Whenever you have a lot of school districts you are going to have a lot of variation in the wealth of the districts because wealth is not distributed in a uniform way. We're also going to try to show that the wealth disparity is increasing over time. It's getting worse, and worse. The larger the variation is, the harder the school finance system has to work to overcome it.

Second, we're going to show that the per pupil spending of the school districts varies dramatically from one place to another. We will raise questions about why it is that students in one part of the state are getting the benefit of spending on the order of $5,000 to $7,000 per student, while students in another part of the state are only receiving $2,000 to $3,000 per student. You have to ask the same questions too. "Why is that?" "Why would that be?" "What role does the state play in seeing that those variations don't exist?"

Third, we're going to show that there is a relationship between wealth and spending. That goes back to that fiscal neutrality issue raised in California. We're going to try to show that wealthier districts happen to be the ones that are spending at the higher levels. If we can show that, we will get the court's attention. They don't like to see that.

Fourth, we're going to show that tax rates vary among the districts, and we're going to show that that variation is growing and we're going to show that the tax rates are inversely related to the spending of the districts. That means the higher spending districts actually are the ones that have the lower tax rates. When you start showing those things, then you get the court's attention. Then we're going to get even more specific.

We're going to get into how the districts spend their money. We're going to look for variations in instructional spending, administrative spending, and other functions that are related to the wealth of the districts. Ask yourself, "If I were to look at the state of Nebraska, what would I see?" "Would I see variations in spending, and are they related to the wealth of districts?" We're going to go even further below the surface. We're going to look at the number of teachers employed. We're going to look at how much those teachers are paid. We're gong to look at the qualifications of those teachers in terms of their training and experience, and we're going to try to show the same things we tried to show for everything else.

First of all, are there variations in the state? Are some kids in classes that are small, and some kids are in classes that are big, and some kids are in classes taught by teachers with Masters' Degrees, and some kids are in classes taught by people with Bachelors Degrees? In some classes do teachers have 10 to 15 years of experience, and in other classes do they have two to three years experience? And we're going to load up the record with as many of those variations as we possibly can and we're going to say that it's related to the wealth of the districts. We're going to go further, and look at the number of courses that are offered. We're going to start talking about what courses are available, and whether the courses that are available in this district might also be available in another district. If they're available in this district, we will say it's because they are wealthy. If they're not available here, we will say it's because they are poor. We're going to look at the availability of supplies and materials, things like computers; and we're going to look and see if that varies, and if it's related to wealth. We're going to look at the quality of the facilities; and we're going to try and determine whether the facilities are related to the wealth of the district.

Then we're going to look at particular parts of the state aid system. We're going to look real carefully to see if there are pieces of that system that don't equalize, that are not sensitive to the wealth of the districts, or the needs of the districts. We're going to go right to those parts of the state aid system, that, for example, are flat grants. Anytime the state gives out the same amount of money to everybody, it is not sensitive to the needs of the districts or the wealth of those districts. I can tell you today technology is very different from what it was in the 1960's. Today, we do know what the needs of the pupils and the districts are. We can measure it. We can quantify it. We can bring it into court. We're going to look at the way that the state supports special education, and whether or not it's sensitive to the wealth of the school districts.

Most states provide the same percentage of support to every district, without regard for wealth. We know what that means. It means that the districts have to pay the rest of the money that the state doesn't pay. Wealthier districts have an easier time doing that than poor districts. When we see that, we're going to bring that to the court's attention. We're going to look for any money that's coming in that's unmatched by the state. The larger the proportion of the money that is coming from a local unrestrained source, the more attention we're going to pay to that in court. We're going to look at things like statutory provisions, to see whether or not the law said one thing, but the allocation of money acts in a different way.

Finally, and this is a new point that hasn't been tested very much, but I know that in some of these cases that are going on around the country, it's being looked at. It was involved in West Virginia. It was involved in Kentucky, and that is the question of whether or not the state is providing sufficient support to meet the very requirements that it's placing on school districts. If you can demonstrate that there's not enough money out there to meet the accreditation requirements for the school districts, then you'll also get the court's attention. In the past five years, there's been a lot of time spent improving or increasing the standards that we expect school districts to meet. The question is, have we provided enough money to insure that they can meet them? This is now a point that is being raised in all of these cases.

The situation is not hopeless. Think in terms of your own situation, remember the state also gets a chance to go into court. These are the kinds of points the state typically tries to make. First, the state is going to look at the variations that exist and it will try to explain them to the court. It's going to say to the court, "of course there are spending differences out there, what would you expect in a state where districts vary this much in size? Some districts have to spend more than other districts, it's obvious. Some districts have larger proportions of kids in special education. Some districts have higher transportation costs. What the plaintiffs told you about those spending differences can be explained." What they might say is that the, "explanation for those differences is that our districts choose to spend more money." They tax themselves at higher rates, so that they can spend more, and that's what we call local control. Local control is a hallmark of American education. How could you possibly find that unconstitutional?

The defense (i.e., the state) is going to look at the variations that the plaintiffs raise, and it's either going to explain them by factors which are legitimate, or it's going to say that it's attributable to local control. They're going to show that by demonstrating that there is a relationship between taxing and spending. Then they can say the higher taxing districts are the ones that are spending more. That's why there's the variation.

The next thing they're going to try to show, and this has not proven to be very successful, but they'll do it every time, is that money doesn't make a difference. It doesn't matter how much money is spent, it has nothing to do with pupil performance. Why are we talking about variations in spending, if we cannot show that money is somehow related to how kids do?

Well, think about that. Do you think money is related to how well kids do in this state? Do you think the pupils in districts that spend more do better, or not? Almost no parent that I know of would ever opt for a program with fewer teachers, fewer courses, teachers that were less prepared, with fewer computers, and so on. The courts will typically say that kind of approach is irrelevant. If education is a fundamental right, and if it can be shown that some students don't have the opportunity for a good education, then it doesn't

matter whether money actually makes a difference. What matters is whether everybody has the same opportunity to see whether it makes a difference. It's a tough point to argue, but it's one that's always brought up.

The third thing they'll try to show is that every single district in the state has enough money to meet accreditation standards. Every district is currently meeting standards. There aren't too many states where districts are unaccredited. There are some states where there are multiple accreditation levels. The plaintiffs will try to show that those that meet the lowest level tend to be poor. Those that meet the highest level tend to be rich. The defense will argue that everybody can meet the minimum standards.

The defense will make an argument that education is not a fundamental right. Think about it as a legislator. You're in a state where you're spending half of your budget on education. The people who are defending you in court are saying that education is not a fundamental right of students in the state. It's the best way to assure a win. It's the strongest point that you have to win on, yet it's a point that is difficult to defend. I certainly hope education is a fundamental right. I certainly hope that that's why we devote half of our money to it. And yet to win a case like this you have to argue that it's not.

Finally, they will focus on local control. They will say that the differences are solely due to local control, and local control is the policy end, the goal that we have. They will also argue that that makes the system rational.

What happens when the court gets involved is not particularly good. A lot of things will happen. Let me give you some examples. Typically, results of these court cases is that there will be a trade off between equity and local control. In your system, whether you know it or not, you're trying to pursue three objectives. You're trying to achieve an adequate level of spending; you're trying to achieve some level of equity across the school districts; you're trying to do it at the same time that you're providing local control. By local control, we mean the districts decide how much money they can spend and how they will spend it.

The courts will change the balance of those three things. The pursuit of equity will become much more important, at the expense of local control. I do not know of a situation where, after the court declares a school system unconstitutional, school districts get more local control, or even maintain as much local control as they had before. It's the price that the plaintiffs are willing to pay for more state aid support. Almost every one of these cases provides more state support for education. That's what the plaintiffs are looking for, and they're willing to trade that against a loss of some local control. The state will typically have a greater role in defining what education services are offered and how they are offered. It is not atypical for the state to come in with a much more specific list of what it is that ought to be provided. If you were to look at the West Virginia case, you would see that in action. It may be true in Kentucky. We are not sure what's going to happen there.

When the court gets involved, it increases the likelihood that they'll continue to be involved. New Jersey is currently involved in a law suit. The state where the system was declared unconstitutional in 1973 is still in court. We expect the decision this year, or maybe next year, on whether the system that was put in place actually fulfills what it was the court had in mind 16 years ago. The same was true in Washington. The same was true in Connecticut. Once the court gets involved, it typically is around for the long haul. The other thing that might happen is that the kind of solutions that are acceptable to the courts are what many legislators might label as draconian. They're the kind of things that you wouldn't do; politically they're not feasible.

Wyoming, for example, put in place what some people refer to as a "recapture" provision. It's a system under which every district in the state, and they've only got 49 of them, must have the same tax rate; if that tax rate produces more money than what the state says each district needs, then the difference is sent to the state. That money then goes to other districts where they don't get as much as the state says they need. Most states don't have a very easy time dealing with that kind of solution. But once the court gets involved, that kind of solution may be the only thing that will solve the problem. And when you have

as few districts as a place like Wyoming has and such enormous wealth variations, it truly is the only way to deal with it.

"Finally, there is the question of state taxes. When the court gets involved, it's not unusual for the state tax system to start to change too. The case in point is New Jersey. Many people say that the court in the state of New Jersey required the state to create an income tax, which it had not had before their involvement. In fact, I don't think that's precisely true. The court said, "When you come up with a solution to this problem, you must fund it at a level which is acceptable." The legislature did create a new system. They did not fund it at a level that would make the system work. The court shut the schools down until the legislature found the money. They found the money; it was in the income tax. The court didn't mandate the income tax. They mandated that there be enough money to supply the system. The same thing happened up in Montana, where they talked about a sales tax. It happened in Washington, where that state went through a recession soon after the court case, and could not come up with enough money to fully fund the new system. The court said that system has priority over other areas of funding in the state, and you must fund that first and then you can fund other parts of the system. A similar thing appears in the Texas opinion, which suggests that schools have first priority on money. My point here is that once the court gets involved, they're involved for the long haul, and they'll be involved in ways which nobody would have ever thought possible at the beginning.

"I think the conclusion I draw from all this is that if the formula is the devil, at least it's the devil that you know. But when you get the court involved, then you get the devil that you don't know. You don't know what's gonna happen. You don't know where it's gonna go. It's not a situation that I like to see anybody in. I urge the states that I work with to make sure they know where their systems are, and to make whatever changes they can afford to make, and they feel are necessary to make, to avoid this kind of involvement. Because if you get caught in this one, you'll be there for a long time, in ways that we cannot predict today."

COMMISSION FINDINGS AND CONCLUSIONS

Over the course of some eighteen months and twenty-one meetings, the Commission has made a number of findings and come to a number of conclusions about school finance in Nebraska. Several of the conclusions and findings are of an obvious nature; others are more complex and subtle. The conclusions and findings derived from a number of sources including information shared by Commission members based on their own situation and experience; reports and data compilations of staff members who served the Commission; reports, data and analysis brought to the Commission by experts from outside Nebraska, including some work done for the Commission by John Augenblick, a school finance consultant; and finally testimony and information shared with the Commission at several public hearings held by the Commission during the summer.

School finance has been likened to a Russian novel--complex, hundreds of characters to memorize, boring, and everybody gets killed in the end.2 In one sense, the comparison is valid. The Commission has spent literally hundreds of hours attempting to come to an understanding of the issues involved in school finance. Hundreds of actors--school administrators, teachers, school board members, senators, the Governor's representative and taxpayers--have provided the context and driving forces (often countervailing) which have influenced the Commission as it performed its work. And the Commission, now close to its end, is proposing a set of recommendations which include serious tax policy changes which might cause the weak of heart some fears for their future political life.

Unlike a Russian novel, however, the Commission's meetings have been punctuated by good will, humor and a real desire to come to a clear understanding of a complex topic. There has been a real coalescing of citizens from diverse backgrounds and walks of life.

And in the final analysis, the Commission has been able to agree to some goals which Nebraskans have supported for a long, long time: Reducing the reliance of schools on the property tax and assuring that all students have access to a quality education regardless of where they may live in the state. These goals seem likely to provide more political benefits than political liabilities for supporters.

The Commission's findings fall generally into categories based on two major themes or problems that exist in Nebraska school finance today. The first major problem perceived by the Commission and nearly every other group studying school finance over the last twenty-five years--is that Nebraska relies excessively on the property tax for the support of its public school system. A number of negative effects result from this basic problem including, to mention just a couple, inequities between taxpayers residing in rich and poor school districts and excessive tax rates on property in comparison to rates in other states. These items will be further discussed in the first part of the Commission's findings and conclusions, "The Property Tax Problem."

The other major problem, not as often discussed by politicians and taxpayers but probably a more damaging problem to the state in the long term, is that the current school finance system does not provide any assurance of equitable educational opportunities for students residing in different parts of the state. The Commission has chosen to define this equity problem in terms of school district access to the financial resources which are critical to providing the staff, curriculum and operational maintenance of a school system. The second part of these findings and conclusions "The Educational Equity Problem" will include a discussion of a number of issues related to this basic equity problem in Nebraska's current school finance system.

The Property Tax Problem

Nebraska public schools rely more heavily on property taxes for support than nearly all other states. Conversely, state support for schools is lower than in nearly all other states. Table 1 on page 32 shows that local support (primarily property tax) in Nebraska is in

excess of 70 percent while nationally, local support is just over 43 percent. Table 1 on page 32 also shows state support in Nebraska of just over 24 percent while, nationally, 50 percent comes from the states.

	LOCAL	STATE	FEDERAL
Nebraska	70.3	24.5	5.2
U.S. Average	43.5	50.2	6.3

Table 1. Percent Of Revenue For Public Elementary And Secondary Schools By Government: Source: Data Search, Estimates of School Statistics, 1988-89, National Education Association.

Only one other state, New Hampshire--which does not utilize state sales and income taxes as a revenue source --- provides less state support than Nebraska. (See Appendix D)

Further, Figure 1 below and Figure 2 on page 33 demonstrate that Nebraska state support for schools has been declining while, nationally, the trend has been toward a higher level of state support.

Figure 1. National Comparison of Revenue Sources For Public Elementary and Secondary Schools: 1939-40 to 1984-85: Source: U.S. Department of Education, National Center for Education Statistics, Statistics of State School Systems; Revenues and Expenditures for Public Elementary and Secondary Education; and Center for Education Statistics, "Common Core of Data" survey.

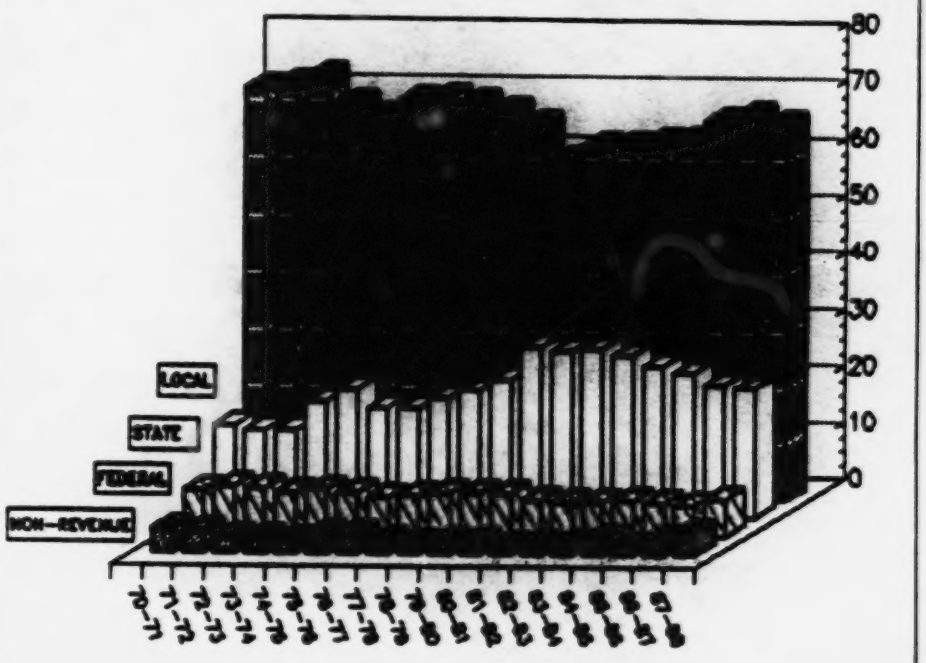

Figure 2. Nebraska Percent Share Of School Revenues From Local, State, Federal And Non-Revenue Sources: Source: Annual Financial Reports of Nebraska School Districts.

Even during the period of greatest state involvement in school reform, (1983-88) Nebraska's state share was actually declining. This occurred despite the fact that the Legislature with LB 994 (1984) actually did mandate a number of "excellence" reforms such as a longer school year, higher graduation requirements, more demanding accreditation standards and tests for beginning teachers, all of which had some cost impacts for school districts. Figure 2 shows this negative state aid trend in Nebraska during the reform era which stands in in stark contrast to the records of the majority of states, including many neighboring states, in which state reform agendas also brought a higher state funding commitment.

The Commission did not approach its task in a vacuum. It was acutely aware of the court decisions for railroads and pipelines which were further narrowing the personal property

tax portion of the property tax base. Data made available to the Commission showed that nearly $1 billion in property tax revenues are lost annually due to property tax exemptions.3 The Commission became even more convinced that the property tax base was too narrow and unstable to continue to support a function as critical to the state and its citizens as children's education. This conclusion further supported the Commission's determination to broaden the tax base in the tax support system for schools.

Taken in isolation, the fact that local property taxes bear the brunt of the tax burden for school support is not consequential. The impact of Nebraska's heavy reliance on the local property tax is what causes the Commission grave concerns. The Commission found that the heavy reliance on property taxes has resulted in highly inequitable tax burdens between taxpayers residing in school districts of similar size where there is a significant disparity in property wealth between the districts. Table 2 shows the example of two Nebraska school districts of similar size with comparable costs per pupil. The levy in District A must be nearly twice as high as the District B tax levy because of the great disparity in property valuations. The Commission has concluded that this type of inequity between taxpayers cannot be justified.

DISTRICT	ENROLL-MENT	COST PER PUPIL	VALUATION (million)	LEVY
District A	445	3319.78	44.4	2.2431
District B	449	3698.29	95.2	1.1540

Table 2. Comparable Costs

Further data from John Augenblick, the Commission's consultant, verifies that as a whole property tax rates have an inverse relationship to property valuation. That is, when property values are low, tax rates tend to be higher. (See Appendix F) This relationship bodes ill for both taxpayers and students in property poor districts.

Figure 3 on page 35 is a graphic representation of the disparity in property rates for Nebraska schools. The chart illustrates a 7 to 1 ratio in property taxes levies at the extremes. This is not tax equity for property taxpayers.

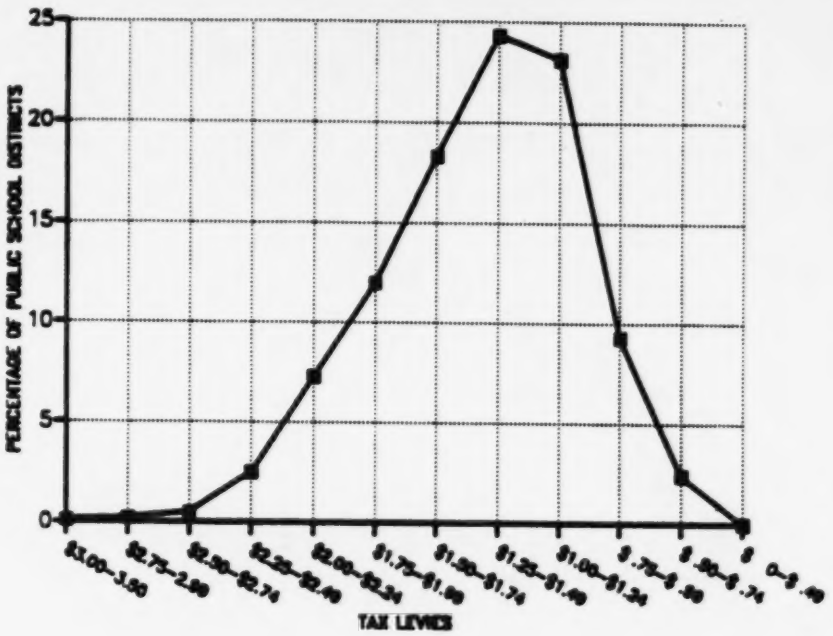

Figure 3. Percentage Distribution of Tax Levies For Public School Districts In Nebraska 1988 - 89: Source: Legislative Fiscal Office.

A second condition arising out of the state's heavy reliance on property taxes is the fact that Nebraska homeowners and farmers pay more than twice the national average in property tax levies. This tax condition, which would seem to be an impediment to economic development efforts for the state, was pointed out to the Commission and the legislative study committees by witnesses at public hearings who compared the property tax costs of owning a home or running an agricultural operation in Nebraska to costs in neighboring states. Tables 3 and 4 on page 37 illustrate the impact of a high reliance on property taxes for home owners and owners of farm real estate. This comparison includes total property tax levies.

	PERCENT
Nebraska	2.29
National Average	1.21

Table 3. Average Effective Property Tax Rates Existing Single Family Homes With FHA Insured Mortgages 1985: Source: State Policy Data Book 88'

	TAXES PER $100 OF MARKET VALUE
Nebraska	1.64
National Average	.71

Table 4. Taxes On Farm Real Estate 1986: Source: U.S.D.A

The Commission came to the conclusion early that a tax shift from the property tax base to a broadened base including state income taxes and sales taxes was advisable. In coming to this conclusion, the Commission noted that spending in Nebraska, both on a per capita (Table 5) and per student (Table 6 on page 37) basis were at or below the national average.

	ELEMENTARY & SECONDARY ED. GEN. EXPENDITURE PER CAPITA
Nebraska	644.83
National Average	644.13

Table 5. Per Capita Spending: Source: Government Finances in 1986-87, U.S. Department of Commerce

	ELEMENTARY & SECONDARY ED. EXPENDITURE PER PUPIL
Nebraska	3,756
National Average	3,977

Table 6. Per Pupil Spending: Source: Secretary of Education's Wall Chart for 1988, U.S. Department of Education.

Thus, since it did not seem realistic to expect major cuts in school spending, a shift to a broadened tax base for schools appeared to the Commission to be the only rational alternative. The Commission further noted that while Nebraska ranks 14th in property taxes and 42nd in sales taxes per capita, overall, Nebraska is near the middle or 27th in total general tax revenues per capita. Figure 4 illustrates this point.

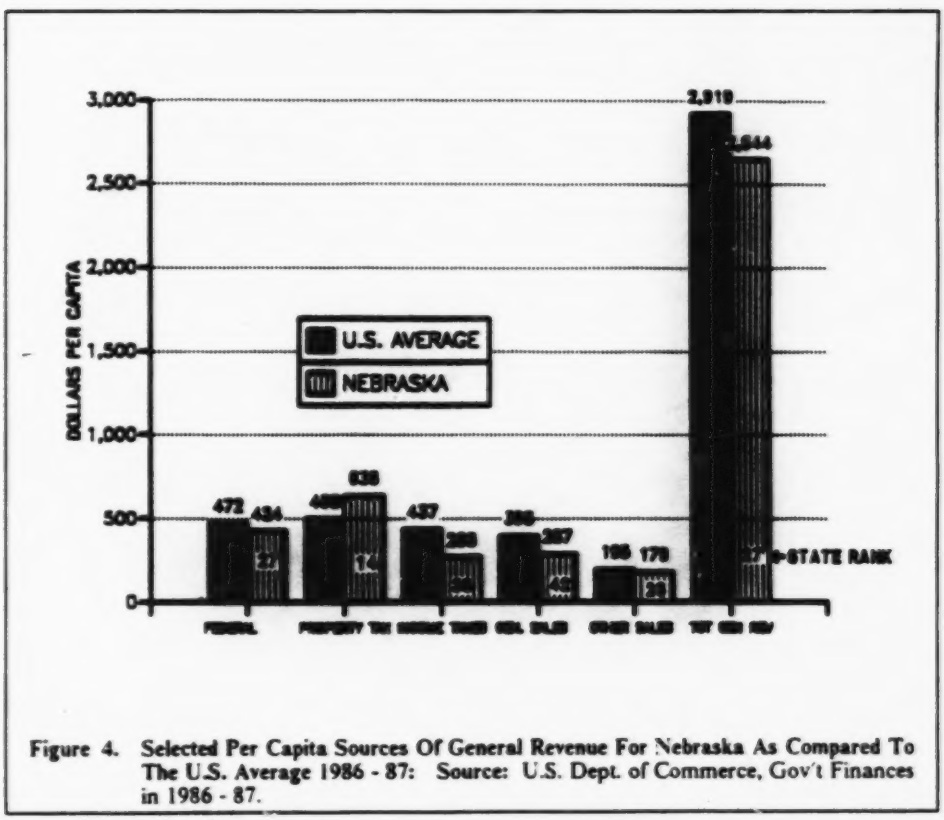

Figure 4. Selected Per Capita Sources Of General Revenue For Nebraska As Compared To The U.S. Average 1986 - 87: Source: U.S. Dept. of Commerce, Gov't Finances in 1986 - 87.

Based upon these understandings, the Commission reached the conclusion that a shift to more state tax support for schools could be accomplished with the overall tax burden per capita remaining fairly constant. It is important to note that this conclusion was based on the assumption that overall spending for schools would remain relatively constant at inflation-adjusted levels.

The Educational Equity Problem

The total costs of operating the public schools for school year 1989-90 will exceed one billion dollars. As noted previously, the state supports only about one fourth of such costs through a variety of sources including: Foundation and Equalization Aid ($133 million), special education ($60 million), School Lands and Funds income ($19 million) and other miscellaneous resources. With the exception of the $33 million funded through the current equalization formula, none of these state resources is paid out to the districts on the basis of school needs and ability to finance needs. The $33 million in the current equalization program (only 3.3 percent of total school costs) was found by the Commission to be completely inadequate to assure any sort of fiscal equity for school districts.

Since one of the important goals for any state aid program is to assure all children an equitable opportunity for an appropriate education, the Commission questioned whether the current system could meet that goal. To use one example, the Commission compared two districts of comparable size and comparable levy. It found, as shown in Table 7 on page 39, that a district's ability to provide the resources for equitable education opportunity can be drastically impacted by the taxable valuation base of the school district. As shown in Table 7 on page 39, District A could afford to spend more than $1,300 per student or about 1/3 more than District B. These represent actual Nebraska school districts. This is not an extreme example.

	ENROLL-MENT	VAL. PER PUPIL	LEVY	COST PER PUPIL
District A	401	255,427	1.4301	4,327
District B	415	95,870	1.6991	3,362

Table 7. Comparable Levies

The Commission's conclusion was reinforced by the analysis of the consultant Dr. John Augenblick who found a moderately strong statistical relationship between school district wealth, as measured by property valuation, and school district spending. This means that a school district's ability to provide appropriate services to its students can be negatively, as well as positively, impacted by the relative wealth of this property tax base; something Nebraska educators have known for a long time. (The statistical analysis by Dr. John Augenblick is found in Appendix F).

As noted in the first part of these findings, there is currently a seven to one ratio or 700 percent difference between the highest and lowest school tax levies in the state. The Commission's consultant, Dr. John Augenblick, found an inverse or slightly negative statistical correlation between tax rates and spending. That is, higher taxing does not generally produce higher spending capability. In other words, some districts must tax much higher than average only to be able to spend much lower than average. It was noted that this is the type of educational equity problem that courts find very troubling. (See the "School Finance and the Courts" section of this report.)

The Commission also noted that the current equalization formula assumes the same needs exist for all schools no matter what the size of the school district. Size of school districts in Nebraska, as across the nation, is a major determinant in costs. This is shown graphically in Figure 5 on page 40.

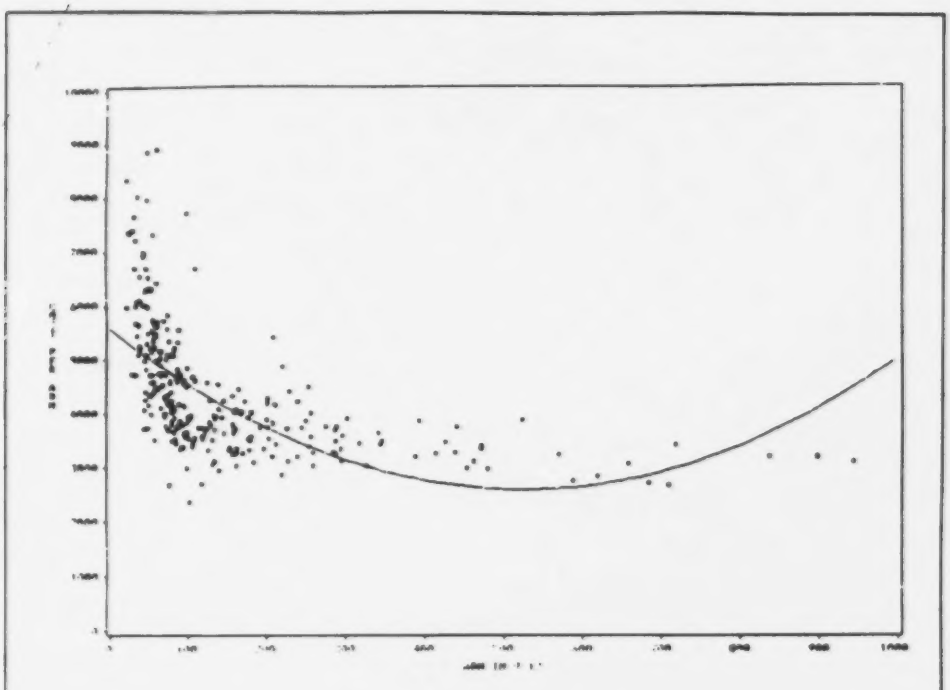

Figure 5. 1986-87 Non-Categorical Cost Per Adm In Grades 9-12: Source: Nebraska Department of Education, Management Information Services, 1989.

As noted in the section describing the current finance and organizational structure of the Nebraska school system, there is tremendous diversity in the size, needs and property wealth of Nebraska schools. To the extent that the current equalization formula ignores the significance that school size plays in determining school costs, an equity problem exists. The Commission came to the conclusion early on that it did not want to use school finance as a vehicle to force school reorganization. It concluded that one must provide the fiscal resources to assure educational opportunities for students in all schools that continue to operate.

Therefore, the Commission found that school districts' need should be based on enrollment tiers of comparable sized school districts. This tiering concept addresses, to a very large degree, the great size diversity which exists between very small Class I and II school districts and the very large Class III, IV and V districts. It meets the Commission's goal of making the new finance plan as "reorganization neutral" as possible. (See Appendix E which describes the tiers recommended by the Commission.)

The Commission's consultant John Augenblick did an analysis which confirmed the Commission's belief that size is the primary and most important element of school costs. The Commission recognizes that other factors such as student poverty levels, sparsity, transportation needs and limited English proficiency do influence school district needs and costs. However, in the interest of maintaining as much simplicity as possible in the distribution formula and with the assumption that these issues may be addressed through future fine-tuning of the proposed system, the Commission concluded it was not in the interest of the state to pursue special need factors in its initial plan.

On a related issue, the Commission did examine the need for separate categorical or incentive programs. A survey of Commission members' preferences for special categorical programs found special education, transportation, wards of the court, gifted, and disadvantaged as top priorities. (Special education and wards of the court are separate categorical entitlement programs funded through distributions separate from the general state aid embodied in the School Foundation and Equalization Act. Transportation, gifted and educationally and culturally deprived are funded through add-on weightings in the current equalization formula.) The Commission also considered its charge to examine whether state aid incentives should be tied to school performance. Recent State Board of Education revisions to Accreditation and Approval Standards which implement a legislative requirement for performance based accreditation and a legislative goal that all public schools become accredited were considered by an incentives subcommittee and the Commission as a whole. The conclusion was reached by the Commission to delay any action in proposing additional incentives or categorical programs. It was felt that these issues, while important, would complicate the Commission's plan and detract from the Commission's primary goals of broadening the tax base for schools (with resultant property tax relief) and assuring more equitable resources and educational opportunities for all students through a sound equalization program.

The Commission was concerned that the proposed equalization formula, which is based to a significant degree on property valuation, not be distorted by inconsistent assessment practices used in different counties and for different classes of property. It found that,

while assessment practices have improved in recent years, there is still a need to assure a level playing field for property assessment before using taxable values in the equalization formula. The Commission's recommendation includes a provision for state review of assessment uniformity and quality prior to distribution of equalization aid.

Finally, in relation to the issue of limitations on the growth of school budgets, the Commission examined several different types of limitations: Limitations tied to increase in personal income; limitations which could be overridden pending special voter notice, public hearings and board of education votes; the flexible equalization-based limitation used in the Kansas system. It also compared increases in educational costs of Nebraska schools to national indexes such as the Consumer Price Index or the Cost of Education Index. Table 8 on page 43 shows examples of these national indexes.

The Commission found that the Kansas type budget limitations would serve the Nebraska school finance system well. It became convinced that budget limitations set annually by the Legislature, based on index data, as well as current revenue and cost projects, would allow for the necessary flexibility to meet constantly changing school needs and state revenue situations.

Fiscal Year Equivalent	Consumer Price Index (1)	Price Index % Change	Public Elementary & Secondary School Index (2)	Price Index % Change
1975-76	161.2	9.1	100	
1976-77	170.5	5.8	109	8.6
1977-78	181.5	6.5	116	6.8
1978-79	195.4	7.7	124	6.8
1979-80	217.4	11.3	135	9.2
1980-81	246.8	13.5	148	9.0
1981-82	272.4	10.4	166	12.2
1982-83	289.1	6.1	182	9.7
1983-84	298.4	3.2	194	6.6
1984-85	311.1	4.3	205	5.9
1985-86	322.1	3.5	220	7.1
1986-87	328.2	1.9	232	5.8
1987-88	340.4	3.7	244	4.7
1988-89	354.3	4.1	N/A	N/A
1989-90 (est.)	371.4	4.8	N/A	N/A

Note: (1) Bureau of Labor Statistics, U.S. Department of Labor.

(2) Statistical Abstract of United States, United States Department of Commerce, Bureau of the Census, 1989.

Table 8. Cost of Education Indicators

The Commission was cognizant of past and current property tax relief efforts by the Legislature which did not include some sort of limitation on local budget growth. As mentioned previously, the Commission came to the conclusion that an effective, yet flexible limitation on school budget growth was the only way to assure policy makers, as well as the public, that a real shift away from property taxes (and consequent property tax relief) would occur.

In support of its goal to assure more equitable access to financial resources to furnish educational opportunities, the Commission concluded that differential limitation rates would be essential to allow lower spending districts the opportunity to "catch up" with higher spending districts.

PURPOSES OF STATE AID TO EDUCATION AND PRINCIPLES OF A STATE AID PLAN

The School Finance Review Commission finds, after review of public school finance in Nebraska, that state funding should support an equitable share of school costs and that any state aid plan should have as its purpose:

1. To assure all Nebraska children more equitable opportunity for an appropriate education.
2. To provide a broad and stable system of financial support for public schools through an appropriate mixture of revenue sources.
3. To provide equalization of fiscal ability and property tax burden among school districts through implementation of an aid distribution formula which includes income as a revenue source for schools and as a determinant of school district wealth.

To further these purposes the Commission believes that:

1. Income should be considered as school district wealth along with property, but only to the extent that it is an "accessible" revenue source to school districts.
2. All school district general fund revenues except federal categorical funds should be accountable in the computation of a state aid formula.
3. Any formula based on property wealth developed to equalize fiscal ability and property tax burden must address discrepancies in the assessment of property values among counties and, if feasible, among classes of property within counties.
4. Grant, incentive, categorical or other classified state funding be made available to schools with justifiable need. Any grant, incentive, categorical, or other classified state funding should be separated from equalization funding formulas and/or equalization funding in order to avoid dilution or contradiction of equalization's purpose.
5. Some means be developed to assure that state funding intended to equalize fiscal ability and property tax burden be used as intended yet retain as much local control on school programs and finances as possible.
6. A permanent school finance commission be appointed to periodically monitor implementation and operation of the formula and the changes in property value assessments, tax laws, and state mandated education programs to avoid unintentional diversion of state aid purposes.

COMMISSION RECOMMENDATIONS FOR A NEW SCHOOL FINANCE PLAN

In order to address the twin problems of over-reliance on property taxes for support of the schools and inequities in the current school finance system, the Commission is proposing a plan for school finance which includes the following basic elements:

1. **Broadening and stabilization of the tax base for schools through dedication of 20 percent of all state income tax receipts and direct return of 20 percent of identifiable resident individual income tax receipts to the school districts where such individuals reside.**
2. **Increase in the overall level of state aid including dedicated income tax revenues, to effectuate an aggregate statewide 15 percent decrease in all property taxes to be levied (or a 20 percent decrease in property taxes to be levied in support of schools); and to provide state funding of schools, from all state sources, at a target level of 45 percent of the aggregate operational costs of the schools.**
3. **Implementation of a new equalization formula for state aid which is based on the realistic needs of schools and which considers all accessible resources of schools, including income tax revenues returned to the schools, and which is sensitive to the income wealth of school districts, as well as to the property tax wealth of school districts.**
4. **Implementation of rational and effective growth limitations for school budgets which are sensitive to local differences yet assure a substantial level of property tax relief.**
5. **The Commission also recommends that the proposed school finance plan be funded on an ongoing and sustainable basis from appropriate increases in state sales and/or income taxes as determined necessary by the Legislature.**

Income Tax Rebate and Dedication

a. It has been often noted that public schools rely on an excessively narrow and, therefore, often unstable property tax base for their primary support. In searching for mechanisms to address this narrow base problem the Commission early took note of the Kansas finance model which includes a return of 20 percent of individual income taxes collected by the state to the school district

where such income taxes originated. This "rebate" process is a simple way to broaden the revenue base of each school district to include a more dynamic and economically sensitive form of citizen wealth. Based on comparison in the growth of income, sales and property taxes over a ten year period, it was apparent to the Commission that the property tax did not have the elasticity or growth potential to keep pace with increasing school costs without substantial tax rate increases. Thus, the first element of this recommendation is that:

Twenty percent of all individual income tax receipts, net of credits and refunds, should be returned directly to the school district where the individuals reside who have remitted such taxes to the state.

The result is that each school district will have an income tax base upon which it will be able to depend on a continuing basis and will also continue to have access to the property tax base. (As noted below, this balancing of income wealth and property wealth will also play a key role in the proposed equalization formula.)

Based on previous tax year data for each school district as determined by the tax commissioner, the Department of Education will compute each district's allocation of individual income tax revenues. Class I and Class VI school districts and county nonresident high school tuition funds will receive a prorata share of tax receipts from individuals residing in these overlapping districts based on the grades for which such entities are legally responsible. (For example, a Class I in a Class VI legally responsible for education in grades K-6, would receive about 45 percent of the income tax proceeds and the Class VI would receive the remaining 55 percent of the income tax proceeds). Further, in districts with less than 10 taxpayers, the receipts would be commingled and distributed to such districts based on prorata share of taxable property valuations. This is done to protect confidentiality of income tax payers.

Income tax funds would be distributed to school districts by the Department of Education, along with equalization aid payments. Note that school districts will

know how much income tax revenues they will receive for the coming school year by the time the Legislature makes its final appropriations and adjourns. (The same would be true for equalization aid. This process would give school districts the revenue data they need for budgeting by mid-summer.)

It is estimated for the state fiscal year and school year 1990-91 between $80 and $90 million would be returned to school districts in this fashion. This amount could increase to about $100 million when the provisions of LB 611 are fully effective (requiring identification of school district before an income tax return is considered complete).

b. In order to assure ongoing state support for Equalization Aid Funding, the Commission also believes that a portion of all state income tax revenues should go for support of the schools, beyond that portion of individual income proceeds which can be identified as coming from a specific school district and which would be returned directly to school districts as just described. The Commission therefore recommends that:

Twenty percent of all projected state income tax revenues, net of refunds, be dedicated to school finance.

As described above, the identifiable portion of 20 percent of resident individual income tax receipts would be returned directly to school districts as one form of state support for schools. The portion of individual income tax proceeds which cannot be identified as income taxes associated with any specific school district, as well as 20 percent of all income tax receipts from all other sources (corporate, non-resident, trusts, etc.), would also be dedicated to school support and remitted to the State Equalization Fund for distribution under the equalization formula as described in the next section.

It is estimated for the state fiscal year and school year 1990-91 that an additional $20 to $30 million income tax dollars will be dedicated for school support in this manner. Thus a total of approximately $120 million dollars in income tax

dollars would be dedicated for public school financial support for the state fiscal year and school year 1990-91.

Property Tax Reduction and State Funding Goal

As a tangible objective of the tax shift from property taxes to state taxes for support of schools, the Commission recommends a 15 percent aggregate reduction in property taxes to be levied (or a 20 percent reduction in property taxes to be levied for school purposes). In light of recent Supreme Court cases and a plea for relief from those who pay the largest proportional share of school funding, the Commission has noted the heavy burden that property taxpayers carry and has intended from the beginning to lessen that load in the best way possible. The commission recognized that this relief will be an aggregate amount of reduction. Not every taxpayer or every school district will see a 15 percent smaller property tax bill.

As part of the recommended shift from property tax support for schools to a broadened support base which includes more reliance on state taxes, the Commission recommends funding from all state sources be maintained at a target level of 45 percent of aggregate school districts' general fund operating expenditures. General fund operating expenditures do not include expenditures from building or bond funds or payments made to financial institutions in repayment of short-term debt. By placing this state funding level at 45 percent the state makes a substantially increased commitment to educational funding.

State funding or support will include the 20 percent income tax rebate to local districts and the new equalization aid as well as other miscellaneous receipts (i.e. special education reimbursements, state apportionment and other state funded programs).

School District Equalization Aid

As clearly shown in the Commission's findings, great disparities exist in school district levies, taxable property wealth and spending. Too often, school district spending is dependent on the school district's taxable property wealth. These disparities became a great concern of the Commission. Even more dramatic are the great disparities in tax levies for school support. The formula described below is proposed to address and lessen such disparities.

The Commission recommends a "foundation support level"4 type of equalization aid distribution formula which rests on the assumption that the state should assure equalized funding for each student attending public school in Nebraska up to a reasonable and current need level after deducting all accessible school district resources.

The elements of the formula are many but the basic concept is simple: Needs less resources equals state aid. Table 9 on page 51 which follows this section of the Commission's recommendations is a schematic representation of the proposed formula. Some important components of the formula which merit some explanation include the following:

> The needs level or support level per student will be based on actual historical expenditures of schools of comparable size incurred in providing educational services to students. Unlike the current equalization formula, this method of establishing the fiscal needs of schools assures that the state will be funding at a level per student which closely reflects actual current cost.
>
> ...School district formula needs will be based on the actual spending established through creation of seven enrollment tiers for elementary grades and nine enrollment tiers for high school grades. This tiered need approach assures that size factors influencing cost are adequately taken into consideration. (See Appendix E)
>
> ...Need levels per student are computed for all students in each school by reference to each district's enrollment in relation to the mid point or average enrollment of the tier groups. This linear transition is important because it assures that addition or loss of one or two students will not mean great changes in state aid.
>
> ...Resources which are held accountable against school district needs will include the amount derived by applying a statewide local effort rate times the taxable valuation of each school district. The local effort rate will be the variable in the formula which will be calculated annually based on legislative appropriations, school district needs and other accountable

resources. It is important to understand that school districts need not actually levy a tax equal to the local effort rate in order to qualify for equalization aid. It is equally important to understand that the local effort rate is not a maximum levy. School boards retain the authority to make budget decisions based on local needs and desires. The local effort rate is simply used in the formula calculation of property tax resources.

...Prior to utilization of taxable property values in the formula, adjustments could be made to property values by the State Department of Revenue when necessary to guarantee that valuation is based on the best available assessment practices. Adjustments could, if necessary, be made for each school district for each class of property located therein. Adjustments could be based on sales assessment ratios, targeted appraisals or other assessment techniques. The purpose of this provision is to ensure a level playing field in the area assessment of taxable property so that no school district will be unfairly benefited or penalized by assessment practices which are inconsistent across county lines. These adjusted values will be used only for computation of state aid distribution.

...One hundred percent of income tax "rebate" dollars which each school district receives, as described in the previous recommendation, will be held accountable as an accessible resource against the district's needs. As indicated previously, providing each school district with direct access to the income tax base will not only broaden the tax base for schools and assure some greater stability in funding, it will also provide a balance, to a certain degree, to school district property wealth.

...Inclusion of income revenues within the formula does two very important things. First, it broadens the definition of wealth to include an income element in addition to the traditional property valuation element. (Since both property taxes and income taxes are accessible to schools under this proposal, this broadening of the wealth definition is logical and consistent within the context of a school aid formula.). Second, it assures that, regardless of income or property wealth, every student will be guaranteed access to education funded at a base foundation or "Needs" level. Thus, districts which are "poor" in both property and income wealth will receive substantial state equalization assistance. Districts which are "poor" in one form of wealth (income or property) and "richer" in the other form of wealth will tend to have a balanced and stronger local support base and qualify for somewhat less state equalization assistance.

...The Commission plan holds accountable all general fund revenues of school districts except federal categorical revenues. The Commission felt strongly that all monies which help support the general operations of school district are a form of accessible school district wealth which should be considered in offsetting school district needs. Two of the important revenues which would be included are nonresident high school tuition and federal Impact Aid to the extent allowed by federal law. While these are not large revenue sources on an aggregate basis, they are extremely significant for some school districts. A complete list of other actual receipts and their numerical values may be found in Appendix C.

...A continuing school finance committee will be established to monitor implementation of the proposed formula, evaluate the success of the plan in meeting the commission goals and to propose refinements.

NEEDS	-	RESOURCES			=	EQUALIZATION AID
Determined by Actual Expenditures of Comparable-Size School Districts		**Local Property Tax Resources**	+ **State Income Tax Rebate**	+ **Other Actual Receipts**		
• Computed separately for elementary and high school grades. • Actual expenditures are controlled through a budget limitation process.		Yield from Local Effort Rate Levy*	Each district would receive a portion of the state income taxes which district residents paid to the State. It is anticipated that this rate would initially be 20 percent of the income tax paid to the State.	• Public Power District Sales Tax • Fines + License Fees • Excess Nonresident High School Tuition • Transportation Receipts • Interest on Local Investments • Other Miscellaneous Local/County Receipts • Special Education • Proceeds from the Temporary School Fund • Insurance Tax Fund • Prorate Motor Vehicle • Other Miscellaneous State Receipts • Impact Aid • Johnson O'Malley • Other Noncategorical Federal Receipts		State Appropriation to offset local needs not met by other available resources.

* Levy would be annually determined based upon level of available state equalization dollars.

Table 9. Nebraska School Financing Review Commission Proposed State Aid Formula Concept

Budget Limitations

The Commission believes that some limitations on the growth of school district budgets are necessary for two primary reasons: a) Without limitations on school budgets it will be impossible to guarantee that increased state aid and support will replace property tax dollars and result in substantial property tax relief. b) Budgets and spending adopted by school boards eventually will become the basis for establishe: :ed" levels in the formula. It is also a Commission recommendation to provide state support for 45 percent of the costs of operating the public schools. It is necessary that some limitations be in effect so the state's commitment will not be a completely open ended one.

The Commission, therefore, recommends that:

> **Limitations on the growth of school district budgets for the operational expenses of the school should be implemented in combination with the new school finance formula and increased state support. The limitations should be flexible to recognize differences in school wealth, voter preferences and unique local circumstances yet effective to assure property tax replacement.**

A number of items are explained below in regard to the limitations proposed by the Commission. While the precise terms of limitations will be adopted by the Legislature to meet future contingencies, the Commission has reached agreement that the limitation should include the following points:

> ...The limitations will apply only to the budgeted operational expenditures of school districts, not to building, sinking, asbestos or other non-general funds.
>
> ...No district will be allowed to increase its budget of operational expenditure more than its allowable growth percentage except as provided below.
>
> ...A range of allowable growth will be established by the Legislature each year based on a number of considerations including available state appropriations and projected increases in costs applicable to schools. Districts spending at or above the average of comparable sized districts will be allowed to increase their budgets a base percentage. Districts which spend less than the average of comparable-sized districts will be able to increase their budgets by an additional percentage up to the top of the percentage range. The Commission recommends a range of 4 percent to 6.5 percent for the initial year of implementation.
>
> ...Upon a seventy-five percent vote of the school board, following special public notice and public hearing, budgets may be increased an additional 1 percent. (For a three member board, three votes in support of an additional 1 percent budget growth; for a six member board, five affirmative votes; for a nine member board, seven affirmative votes; and for a twelve member board, nine affirmative votes.) The limitations may be overridden in any amount by a majority vote of registered voters at a special election called by resolution of a school board or voter initiated petition.

...Schools with greater than specified levels of reserves will budget those as revenues. Those with insufficient reserves will be allowed to increase their reserve to the following levels: Twenty-five percent combined cash reserves, contingency funds and depreciation funds for larger districts serving students in the top quartile and 30 percent, 40 percent and 50 percent respectively for the smaller districts serving students in the remaining three groups.

...Districts experiencing enrollment growth will be allowed additional budget authority. Districts may apply to the State Department of Education for increased budget authority based on projected enrollment increases for the coming school year. The State Board of Education will review and take action to approve or deny applications projecting enrollment increases exceeding prescribed percentage levels applicable to school districts in comparable size groups. Districts experiencing declining enrollment will not lose budget authority since growth limitations are applied to total budgets of operating expenditures, not budgets per pupil.

...Increased expenditures for new or expanded programs as mandated by changes in state or federal law will be allowed.

...School districts will be allowed to save unused budget authority. The Commission believes this provision will prevent the limitations from becoming spending floors.

...Amounts budgeted in excess of the allowable growth will be deducted from future state support payments and will not become part of the budget base for the following year.

State Revenue Sources

The Commission believes one of the major problems inherent in the current school finance system has been the failure to fund schools from a state level on an ongoing, sustainable basis. Increases in aid have been sporadic and therefore have not kept pace with increasing school costs, further pushing the burden of funding the day to day costs of operating the schools onto an already overburdened property tax. Further, the Commission was extremely cognizant of current instabilities in the personal property tax component of the property tax base.

Recommendations 1 and 2 of this plan call for dedication and rebate of a portion of the income tax base, ongoing state funding of 45 percent of the costs of operating the schools and a 15 percent reduction in aggregate property taxes collected in the state or a 20 percent reduction in property taxes to be levied in support of schools. Funding these recommendations will cost money. The Commission believes that funding the plan will require increases in some state taxes. Therefore, it is the recommendation of the Commission to the Legislature:

That the School Finance Review Commission Plan be funded on an ongoing and sustainable basis from appropriate increases in the state sales and/or income taxes as determined necessary by the Legislature.

The Commission felt it was not in the best position to project the budgetary and cash flow needs of the state. This is a function uniquely appropriate to the Governor's Budget Division and the Legislature's Fiscal Office. Final decisions must, of necessity, come from the Legislature and the Governor in light of other budgetary and revenue actions.

The next section of this report, "Fiscal Impact to Fund the Commission Plan", provides policy makers with the cost and revenue assumptions which the Commission used when creating its plan. It is hoped that this information will be useful to the Legislature and the Governor as they proceed to consider the Commission's plan.

FISCAL IMPACT TO FUND THE COMMISSION PLAN

45% State Share

The Commission recommended that state aid be increased to fund 45 percent of the aggregate general fund operating costs of public schools. The Commission proposes that general fund operating expenditures of schools be calculated by utilizing the following line items from the Annual Financial Report for Public School Districts:

Line 296	**TOTAL GENERAL FUND EXPENDITURES**
Less:	
Line 84	Tuition-Other Districts (Regular)
Line 85	Tuition-Other Districts (Special Education)
Line 255	Transportation-Other Districts
Line 279	Summer School Expenditures
Line 288	Adult Education (General Fund)
Line 290	Transfers to School Lunch
Line 49	Transfers from Other Funds
Line 270	Community Services
Line 271	Redemption of Debt Principal
Equals:	**GENERAL FUND OPERATING EXPENDITURES**

Table 10. General Fund Operating Expenditures

The state currently provides aid to school districts through the School Foundation and Equalization Act. Additional revenue from the state is allocated to schools for entitlement programs, such as wards of the court and special education. Rental income for school

lands and interest proceeds are distributed by the state to schools in the form of state apportionment and in-lieu of school land tax payments. State revenue sources also include prorata motor vehicle and insurance premium tax proceeds and homestead exemption receipts. In addition, state funds are provided for school lunch and vocational education programs and beginning in 1989-90 the state is funding a salary enhancement program for teachers. Table 11 on page 57 shows an estimate of the total state aid which will be provided to schools through existing state revenues sources from 1990-91 to 2000-01.

Based on the definition of general fund operating expenditures as previously explained and then projected future state receipts by schools for existing state aid programs, the estimated additional state aid needed in 1990-91 to fund the Commission plan is $211.3 million. The estimated General Fund fiscal impact of the Commission plan for the state from 1990-91 to 2000-01 based on the following assumptions is shown on the Table 12 on page 58.

Target Percentage of Expenditures	45.0%
Spending Growth (FY88-89)	6.0%
Spending Growth (FY89-90)	9.0%
Spending Growth (FY91 & Beyond)	5.0%

Wards of the Court	5.0%
School Lunch	5.0%
Special Education	6.0%
State Apportionment	6.0%
In-Lieu of School Level Tax	6.0%
Process Motor Vehicle	5.0%
Insurance Premium Tax	5.0%
Structural Exception	2.0%

	FY1987-88	FY1988-89	FY1989-90	FY1990-91	FY1991-92	FY1992-93	FY1993-94	FY1994-95	FY1995-96	FY1996-97	FY1997-98	FY1998-99	FY1999-00	FY2000-01
State Aid to Education	120,861,960	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100	133,616,100
Teachers Salaries (1988)	0	0	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000
Wards of the Court	2,223,010	3,211,916	4,670,000	4,804,432	5,040,000	5,292,000	5,556,600	5,834,430	6,126,152	6,432,489	6,754,082	7,091,786	7,446,375	7,818,694
School Lunch	671,249	661,000	888,581	899,951	881,079	980,632	988,114	985,230	1,804,488	1,895,216	1,140,527	1,197,553	1,257,431	1,320,302
Other state appropriations	650,648	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000
Special Education	57,160,527	64,473,000	68,729,294	76,228,375	82,126,648	88,912,777	96,025,790	103,787,853	112,004,680	120,964,853	130,642,809	141,093,402	152,380,874	164,571,344
Vocational education	105,605	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911	122,911
State Apportionment	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799	14,136,799
In-Lieu of School Level Tax	4,981,771	5,382,797	5,990,785	5,935,752	6,291,896	6,669,410	7,069,574	7,493,748	7,943,374	8,419,976	8,925,175	9,460,685	10,028,326	10,630,026
Process Motor Vehicle	2,188,768	2,299,257	2,414,220	2,534,931	2,661,678	2,794,762	2,934,500	3,081,225	3,235,286	3,397,050	3,566,903	3,745,248	3,932,511	4,129,136
Insurance Premium Tax	10,391,960	10,911,557	11,457,146	12,030,003	12,631,503	13,263,078	13,926,232	14,622,544	15,353,671	16,121,355	16,927,422	17,773,794	18,662,483	19,595,607
Structural Exception	15,713,345	16,500,000	17,300,000	17,400,000	17,700,000	18,000,000	18,360,000	18,727,200	19,101,744	19,483,779	19,873,454	20,270,924	20,676,342	21,089,869
Total Aid from State Source	239,089,549	251,715,417	278,856,785	287,719,853	295,470,611	303,801,489	312,786,829	322,439,050	332,775,030	343,881,496	355,805,412	368,609,202	382,360,153	397,130,789

Table 11. Calculation of Existing State Aid to Schools

Target Percentage of Expend.	45.0%
Spending Growth (FY88-89)	6.0%
Spending Growth (FY89-90)	9.0%
Spending Growth (FY91/Beyond)	5.0%

	FY1990-91	FY1991-92	FY1992-93	FY1993-94	FY1994-95	FY1995-96	FY1996-97	FY1997-98	FY1998-99	FY1999-00	FY2000-01
TOTAL GENERAL FUND EXPENDITURES	1,188,089,331	1,246,493,797	1,307,818,487	1,372,209,411	1,439,819,882	1,510,810,876	1,585,351,420	1,663,618,991	1,745,799,940	1,832,089,938	1,922,694,434
Tuition-Other Districts (Regular)	(5,988,611)	(6,288,042)	(6,602,444)	(6,932,566)	(7,279,194)	(7,643,154)	(8,025,312)	(8,426,577)	(8,847,906)	(9,290,301)	(9,754,816)
Tuition-Other Districts (Spec Ed)	(5,407,403)	(5,894,068)	(6,424,536)	(7,002,744)	(7,632,991)	(8,319,960)	(9,068,756)	(9,884,944)	(10,774,589)	(11,744,302)	(12,801,289)
Transportation-Other Districts	(102,117)	(111,308)	(121,326)	(132,245)	(144,147)	(157,120)	(171,261)	(186,674)	(203,475)	(221,788)	(241,749)
Summer School expenses	(1,904,725)	(1,999,962)	(2,099,960)	(2,204,958)	(2,315,206)	(2,430,966)	(2,552,514)	(2,680,140)	(2,814,147)	(2,954,854)	(3,102,597)
Adult Education (General Fund)	(1,030,070)	(1,081,573)	(1,135,652)	(1,192,435)	(1,252,056)	(1,314,659)	(1,380,392)	(1,449,412)	(1,521,882)	(1,597,976)	(1,677,875)
Transfers to School Lunch	(19,734,686)	(20,721,420)	(21,757,491)	(22,845,366)	(23,987,634)	(25,187,016)	(26,446,367)	(27,768,685)	(29,157,119)	(30,614,975)	(32,145,724)
Transfers from other Funds	(2,193,609)	(2,303,290)	(2,418,454)	(2,539,377)	(2,666,346)	(2,799,663)	(2,939,646)	(3,086,628)	(3,240,960)	(3,403,008)	(3,573,158)
Community Services	(608,877)	(639,321)	(671,287)	(704,851)	(740,093)	(777,098)	(815,953)	(856,751)	(899,588)	(944,568)	(991,796)
Redemption of debt principal	(42,080,827)	(44,184,868)	(46,394,112)	(48,713,818)	(51,149,509)	(53,706,984)	(56,392,333)	(59,211,950)	(62,172,548)	(65,281,175)	(68,545,234)
GENERAL FUND OPERATING EXPENDITURES	1,109,038,405	1,163,269,944	1,220,193,226	1,279,941,053	1,342,652,706	1,408,474,256	1,477,558,886	1,550,067,229	1,626,167,726	1,706,036,990	1,789,860,195
Target Percentage	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45
Total State Support Needed	499,067,282	523,471,475	549,086,952	575,973,474	604,193,718	633,813,415	664,901,498	697,530,253	731,775,477	767,716,645	805,437,088
Existing state aid	(287,719,853)	(295,478,611)	(303,801,469)	(312,786,829)	(322,428,050)	(332,775,020)	(343,881,496)	(355,805,412)	(368,609,202)	(382,360,153)	(397,130,789)
ADDITIONAL STATE AID NEEDED	211,347,429	227,992,864	245,285,483	263,186,644	281,765,668	301,038,396	321,020,002	341,724,841	363,166,275	385,356,493	408,306,299

Table 12. Calculation of Additional State Aid Needed

Effect On Property Taxes

The Commission stated a goal of effectuating an aggregate statewide 15 percent reduction in property taxes levied through the provision of state aid to fund 45 percent of the general fund operating expenses of schools. The following graph compares what the average aggregate property tax levy would be from 1990 to 2000, assuming a 6.5 percent growth in taxes levied, to what the average aggregate property tax levy would be for the same time period if the Commission's plan is adopted, implementing additional state aid and budget limitations which would allow an approximate 5 percent growth rate in property taxes levied for schools.

The graph shows that the average aggregate property tax levy will decrease in 1990 from an estimated 2.683 per 100 dollars of value without the Commission plan to 2.251 per 100 dollars of value if the Commission's school finance proposal is adopted. The total amount of property taxes that will be levied statewide in 1990 is projected to decrease by 16.1 percent if the 45 percent state funding target is achieved. Appendix G contains the data used to compare the effect of the Commission plan on property taxes.

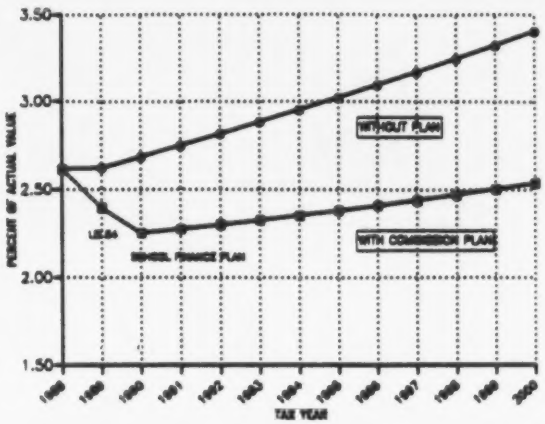

Figure 6. **Average Property Tax Levies With And Without The School Finance Review Commission Plan:**

State Aid as % of School Spending	45.0%
Growth in Property Valuations	4.0%
Growth in Taxes Levied	6.5%
Growth in Taxes Levied With Cap *	5.5%

* Assuming a 5% growth in property taxes for schools due to the impact of the cap, the TOTAL property taxes levied should be reduced from a 6.5% average growth to 5.5% average growth.

Funding Mechanisms

The Commission recommended that its plan be funded on an on-going and sustainable basis from appropriate increases in state sales and/or income taxes as determined necessary by the Legislature. The following tables show the state revenue forecast made by the Nebraska Economic Forecasting Advisory Board (NEFAB) in October 1989 for fiscal years 1989-90 and 1990-91. The projections for 1991-92 are unofficial preliminary planning estimates calculated by the Legislative Fiscal Office (LFO). The Forecast Board will meet again in February 1990, at which time the board will review current estimates.

	Forecast Board Estimate		Preliminary LFO Estimate
	1989-90	1990-91	1991-92
Sales (4 cents)	455.0	470.0	491.2
Individual Income	485.0	515.0	553.6
Corporate Income	75.0	75.0	76.7
Miscellaneous	138.0	130.0	124.3
TOTAL	$1,153.0	$1,190.0	$1,245.8

Table 13. Net Revenue Estimates: State General Fund in Millions

	Forecast Board Estimate		Preliminary LFO Estimate
	1989-90	1990-91	1991-92
Sales tax: 1 cent Increase	113.5	117.5	112.8
Individual Income*: Primary Rate Changes from 3.15 to 4.15	153.9	163.5	175.7
Individual Income: 20% Rate Increase	97.0	103.0	110.7
Corporate Income: 20% Rate Increase	15.0	15.0	15.3
Note: *Primary rate from 3.15% to 4.15%. Note that corporate income tax rates are linked to the individual income tax rates, i.e., on the first $50,000 of taxable, the rate is 150.8% of the primary rate and 211% of the primary rate on the excess. Maintaining this linkage with a primary rate increase of 1% on the individual income results in corporate increases as follows in the next table.			

Table 14. Estimated Rate Increase Impacts in Millions

1989-90	1990-91	1991-92
$23.8	$23.8	$24.3

Table 15. Corporate Income Tax Increases

The Commission recognizes the sustainability of the funding sources chosen to implement the proposed plan is important to insure that the 45 percent target level for state support of public schools is maintained. The following chart illustrates the varying growth rates of tax sources for the state General Fund from 1981-82 to estimates for 1991-92. Also included on the table are growth rates in total property taxes levied from 1981 to 1989 estimated.

Fiscal Year	Sales/Use Tax	Ind. Income	Corp. Income	Misc. Receipts	Total	Tax Year	Property Taxes Levied
FY1981-82	5.0%	10.7%	(10.4%)	6.2%	6.1%	1981	9.04%
FY1982-83	2.6%	11.8%	(28.0%)	(11.8%)	1.7%	1982	6.03%
FY1983-84	6.0%	4.4%	14.6%	7.0%	6.0%	1983	8.95%
FY1984-85	4.7%	6.9%	(23.1%)	5.6%	5.8%	1984	6.13%
FY1985-86	(1.1%)	8.3%	(25.2%)	(6.1%)	0.4%	1985	6.96%
FY1986-87	2.0%	7.3%	4.5%	5.1%	5.2%	1986	4.28%
FY1987-88	7.7%	6.4%	21.9%	(2.0%)	7.0%	1987	3.86%
FY1988-89	10.4%	16.5%	26.5%	3.8%	13.3%	1988	6.04%
CURRENT REVENUE PROJECTIONS (October 1989)							
FY1989-90 NEFAB est.	6.0%	6.4%	(0.2%)	1.8%	5.2%	1989 (est.)	12.00%
FY1990-91 NEFAB est.	3.2%	6.2%	3.9%	2.7%	4.5%		
FY1991-92 LFO est.	3.9%	7.1%	1.8%	2.0%	5.0%		
HISTORICAL AVERAGE:							
Actual Eight Years (FY82 - FY89)	4.2%	9.9%	1.1%	6.8%	5.4%		
Ten Yr. Avg. with est. (FY82 - 91)	4.3%	8.7%	(1.2%)	(0.5%)	5.0%		
Ten Yr. Avg. (FY78 - FY89)							6.5%

Table 16. Growth Rates In General Fund Revenues (Adjusted for Rates, Legislation, One-time Items)

1990-91 Fiscal Impact

In summary, if the commission plan is implemented in 1990-91, the fiscal impact to the state will be $211.3 million to fund 45 percent of the aggregate general fund operating expenditures of school districts. This will be funded in part by allocating $118 million of projected state individual and corporate income tax receipts to school districts through the proposed formula in the form of a 20 percent income tax rebate and equalization aid. Additional funds must be added to the equalization formula to reach the 45% goal. The total amount of property taxes levied in 1991 is projected to be 16.1 percent less than the estimated taxes without the plan.

There are numerous funding scenarios using sales and/or income tax increases, an expanded sales tax base or new tax initiatives which can be utilized by the Legislature to fund the Commission proposal and sustain its implementation in future fiscal years.

END NOTES

1. A volume of supplemental materials which include data describing the items listed and other information prepared and presented to the Commission will be made available to individuals upon request.

2. The "Russian novel" analogy was made to the Commission at a presentation on October 4 of this year by the school finance consultant, Dr. John Augenblick. Dr. Augenblick attributes this analogy to Charles Brown, Director of the Colorado Legislature's Division of Legislative Services. Mr. Brown was the staff person providing the Colorado Legislature with much of the statistical support for its recently enacted (1988) school finance plan.

3. Pages 8-22 and 8-23, Nebraska Comprehensive Tax Study, July, 1988, Syracuse University.

4. Nationally, the term "foundation support level" or "foundation formula" refers to a specific type of equalization formula whereby the state, through state aid, assures that each district will be able to provide students with a basic or foundation level of educational services. Many foundation formulas in other states include foundation support levels which are prescribed by the Legislature; for example at $3,000 per student or $50,000 per class room unit. The formula proposed by the Commission would set the foundation support level or "formula need" level at an average of the actual costs of school districts of similar size for a specified prior school year.

   This type of formula should be distinguished from the current "foundation aid" formula found in current law. Foundation aid in Nebraska is not an equalization aid at all, but rather a flat grant per pupil paid out regardless of the resources or wealth of the school district.

   The foundation support level type of equalization formula should also be distinguished from "power equalization" or "guaranteed yield" type of equalization formula. In the former, the state only provides equalization of resources up to a level--the foundation support level. Districts may, of course, choose to spend more per pupil than the foundation support level and if they do, the extra costs will be funded entirely by the local property tax. Power equalization or guaranteed yield formulas take equalization an added step whereby the state actually provides assistance to districts for per pupil spending above any sort of specified support level. The Kansas formula is a power equalization formula which uses each district's actual budgeted expenditures as the need level of each district. Depending upon each district's budget per pupil in relationship to other districts of similar size, the State of Kansas provides some equalization aid for each dollar actually budgeted by school districts for the operational expenses of students. The Commission concluded that it would be difficult to justify a power equalization formula in Nebraska because, with over 850 school districts of vastly different size, geography, and socioeconomic status, there are also tremendous differences in spending, some of which are justified and some which are not (in terms of identifiable cost factors).

Appendix A. Outline Of State Aid Legislation History in Nebraska

OUTLINE OF STATE AID

LEGISLATION

Prepared by

Corey Phillips
Legislative Aide to Senator Roger R. Wehrbein

August 1988

65-A

Territorial Laws

The school laws required each district to issue a tax levy of 2 mills to support its schools and the state would also match this levy. The money collected would be distributed on a per pupil basis.

1867

Money from the sale of school lands were to be put into a state school fund. This fund was then to be disbursed each year to the several organized counties based on the number of children between 5 and 21 years of age.

1881

The State Common School Fund was enacted to "afford the advantages of free education to all the youth of this state." The revenue collected from the sale of school lands, fines and forfeitures were to be placed in this new fund. In addition, the state tax levy of 2 mills was raised by 1¼ mills and would be distributed semi-annually to the several counties of the state "in proportion to the enumeration of scholars, and be applied exclusively to the payment of teachers' wages."

The county treasurers were then to distribute the fund by the following formula: ¼ evenly to the counties school districts and the rest is payed out on a per pupil basis.

1907

This is the first piece of legislation to be listed under the heading of state aid to schools. If a school district was unable to meet its obligation of holding classes for a least 7 months a year in grades 1-8, and it was at the maximum levy, then the state would offer financial assistance.

The amount could not exceed $125 in any one year and this money could only go for a teacher's wages.

1909

The length of required school term was reduced from 7 to 5 months to qualify for state assistance. The ceiling per year was increased to $275 and $75,000 was appropriated to fund the aid.

1915

The Nebraska Legislature passed several key school measures in this year.

The first, would allow school districts to borrow money to purchase school sites and to erect buildings. Two-thirds of a districts residents attending a bond hearing would have to agree for approval of a bond.

The second, were measures that provided aid to consolidated districts and rural high schools to provide vocational education. Consolidated districts that have a least 25 sections of land and maintained suitable facilities, along with rural high schools were electable for $350 annually to offer agriculture and home economics instruction.

1927

The state increased the period of time a school must be open from 5 to 9 months to be able to receive assistance, but the district must have a levy of at least 8 mills.

1935

Relief was provided to school districts during 1935-36 unable to maintain a normal term after making a maximum effort to do so. Money to assist these needy district came from the Federal Government. The state had $30,000 to compensated any burden on a district as the result of moving families with school age children due to the federal farmstead rehabilitation program.

1945

LB 4-appropriated $10,000 to the Superintendent of Public Instruction from the State's general fund in order to cover necessary expenses of implementing the National School Lunch Act.

1955

LB 304-the excess cost of education of handicapped children would be paid by the state: (1) physically handicapped children would receive $400, and (2) educationally handicapped children are entitled to $200.

1961

LB 411-provided state aid for the special education of the mentally handicapped. Per pupil cost is computed by dividing operational cost, including 3% depreciation cost of the school plant, by number of students enrolled.

1965

LB 274-appropriated funds for local Driver Education Programs. State pays for actual cost or $30 for each student taking a driving course, which ever is less.

1967

LB 448-created the School Foundation and Equalization Act

1967

LB 667-appropriated $20 million dollars to implement the School Foundation and Equalization Act.

1969

LB 467-added $10 million to regular appropriations for state aid; increased foundation aid levels; lowered qualifying levies and clarified that Equalization aid was to be distributed after Foundation and Incentives were funded.

LB 633-deleted Federal Impact Aid as an accountable receipt in the equalization formula.

1971

LB 179-provided for payment of state funds for educating handicapped and emotionally disturbed children to equal actual cost of district.

LB 426-added an enrollment increase factor to the equalization formula; changed schedule of payments

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1972

LB 1167-increased aid to school districts proportionately with increase in membership of one-half of one percent or more. Previously, it took an increase of 5 percent to see an equal increase in state aid.

1973

LB 102-provided for care and education of multihandicapped children at state expense

1975

LB 555-provided financial assistance to school districts for resident handicapped children receiving special educational services

1976

LB 903-changed payment dates of distribution of special education and general state aid funds

1977

LB 477-provided an additional $2.5 million in financial aid to school districts based on ADM (average daily membership)

LB 33-changed amounts of financial support and imposed spending limits, excluded some programs in calculating state obligations and increased the amount of state support. This measure was removed by referendum.

1978

LB 757-redirected a portion of appropriations for distribution of state aid into a formula based on ADM

1980

LB 486-changed the method of distributing funds in the School Foundation and Equalization Act; ratios by grade grouping replaced dollar figures per grade level; foundation aid to be paid to the nonresident tuition fund for high school students residing in Class I districts;aid made payable only for resident enrolled students; and capped the amount deductible as tuition receipts at 125% in the equalization formula.

1981

LB 318-changed schedule of state aid payments; allowed for early payment of aid in hardship cases; added a declining enrollment factor in the equalization aid formula; deducted a percentage of aid for students enrolled in technical community colleges.

1982

LB 816-distributed $70 million in state aid to political subdivisions, including public schools, in lieu of personal property tax replacement dollars previously distributed under unconstitutional formulas.

LB 933-changed the schedule of payment of state aid

1986

LB 419-capped increases in aid payable due to the enrollment increase factor at 10%

LB 757-changed provisions for school district membership reports and aid determination to allow schools to report resident enrollment in January to take advantage of rapidly increasing enrollment.

1988

LB 940-created the School Finance Commission; the qualifying levy for equalization aid for Class I and Class VI school districts were made equal to the qualification levy for K-12 districts.

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Appendix B. 1989-90 Nebraska State Aid To Education Program

1989-90 NEBRASKA STATE AID TO EDUCATION PROGRAM

Summer, 1989

The state aid formula has three main components. In 1989-90, the amount of money distributed in each area is noted below:

Foundation	$ 96,376,100
Incentive	3,649,748
Equalization	33,590,252
Total	$ 133,616,100

Statutes governing the state aid program are found in Sections 79-1334, et. seq. of the Nebraska Revised Statutes. The appropriation bill affecting school district allocations was LB 813 from the 1989 legislative session.

FOUNDATION AID

Foundation aid is based upon resident enrollment in school districts. As per statutory requirements, allotments are computed on a weighted basis that differentiates among various enrollment categories. Ratios associated with those categories are as follows: (1) Kindergarten = .5; (2) Grades 1-6 = 1.0; (3) Grades 7-8 = 1.2; (4) Grades 9-12 = 1.4. The chart listed below indicates figures that were the basis of payments in 1989-90.

*State Resident Enrollment			Calculation Factors		Adjusted Resident Enrollment
Kindergarten	22,858	x	.5	=	11,429
Grades 1-6	128,004	x	1.0 [base rate]	=	128,004
Grades 7-8	38,780	x	1.2	=	46,536
Grades 9-12	77,327	x	1.4	=	108,258
			Total		294,227

The appropriation for foundation aid was divided by the total adjusted resident enrollment to determine the amount of money that would be distributed per student at the base point; i.e., Grades 1-6. The following outline presents a summary of those calculations:

$96,376,100	÷ 294,227	= $327.55†
Kindergarten	@ .5	= 163.77
Grades 1-6	@ 1.0	= 327.55
Grades 7-8	@ 1.2	= 393.06
Grades 9-12	@ 1.4	= 458.58

*1988-89 Data

†Adjusted to show impact at state level. Rounding factor affects figure used for each district.

INCENTIVE AID

School districts will receive some funds for offering Summer School programs and employing teachers with certain college degrees. The payment schedule for both factors is as follows:

Teachers

Bachelor Degree	$150 per person
Masters Degree	$250 per person
Doctoral Degree	$350 per person

Summer School (90 Hours)

Twenty cents per student hour for each participating student

The total amount of incentive aid distributed in 1989-90 will be $3,649,747. Of that amount, school districts will receive $118,602 for Summer School programs. The remaining amount, $3,531,145, is generated through the college degree attainment level factor.

EQUALIZATION

After foundation and incentive aid allotments are determined, the balance of the state aid appropriation becomes equalization aid. In 1989-90, equalization aid will amount to $33,590,252. Equalization payments are based upon a comparison of school districts' assumed needs with their assumed capacity to finance their costs.

Need Factor(s)

The basic need factor for school districts was created by using a derived need figure in the calculations. The weighted need figures in 1988-89 are:

Kindergarten	@ .5	= $ 528.49
Grades 1-6	@ 1.0 [base rate]	= 1,056.99
Grades 7-8	@ 1.2	= 1,268.39
Grades 9-12	@ 1.4	= 1,479.79

After multiplying a school district's student resident population by the above-noted figures, the total need factor for the district could have been enhanced by the conditions cited below:

- If a district transported students in excess of four miles, those students were counted as one and one-fourth students.
- When a district provided a special program for Gifted and Talented Students, those students were counted as one and one-fourth students.
- Students enrolled in a special program for the Culturally and Educationally Deprived were counted as two students.
- In school districts that had a census population that ranged from four people to one person per square mile, the assumed basic need was increased from 10 percent to 40 percent respectively on a sliding scale.

- Changes in school district enrollment affected the formula when: a) Membership increased one-half of one percent or more than the membership of the year prior to the preceeding year. In such cases, the total financial support pursuant to 79-1336, basic needs, increased by the percentage of increase up to a maximum of ten percent. b) Membership decreased more than two percent. The basic needs of those districts were increased by the difference between two percent and the percentage of decrease up to a maximum of ten percent.

Deductible Receipts

Certain accountable receipts were subtracted from the total assumed need figure for each school district during the equalization aid determination process. The following items were considered:

(1) Foundation aid

(2) Property tax yield, as determined by multiplying the district's total valuation by a qualifying levy.
   a) Class I Districts (K-6) = .19 per $100 property valuation
   b) Class I Districts (K-8) = .26 per $100 property valuation
   c) Class II, III, IV, V Districts = .42 per $100 property valuation
   d) Class VI Districts (7-12) = .23 per $100 property valuation
   e) Class VI Districts (9-12) = .16 per $100 property valuation

(3) Other receipts, i.e., State Apportionment, license fees, fines, transportation receipts, Insurance Tax fund, tuition receipts which exceed 125 percent of per pupil costs.

The product of subtracting each district's receipts from its total assumed needs establishes the amount of equalization aid it is eligible to receive. Equalization aid, when all the aforementioned factors are considered, will go to those districts with the greatest comparative need.

The Appendix A of this report contains a listing of documents that were used to build the 1989-90 state aid data file. Appendix B provides a chart of state aid appropriations through the years.

Source: NDE: State Aid Office

DATA SOURCES

The following data sources were used to build the 1989-90 State Aid database:

1988-89	Membership and State Aid Supplement Reports Class of District; Valuation; General Fund Levy; K-12 Total Membership; Kg, 1-6, 7-8, and 9-12 Resident Enrollment; Number of Qualifying Summer School Students, and Organization of District.
1987-88	Membership and State Aid Supplement Repor Number of Regular Tuition Students (Elementary and Secondary); Organization of District; K-12 Total Membership.
1987-88	Annual Finance Report License/Fines, Transportation, Insurance Tax Fund, and Apportionment; Per Pupil Cost-Elementary and Secondary; Regular Tuition Receipts.
1987-88	Annual Statistical Summary College Degree Preparation of Instructional Staff (Doctorate, Masters/6-year/Equivalent, Bachelors); Students Eligible for Transportation Kg, 1-6, 7-8, and 9-12; Population Density Factors
1987-88	Gifted and Talented Student Counts;
1987-88	Culturally and Educationally Deprived Student Counts;
1987-88	Tuition Receipts adjusted for Special Education Nonresident High School Tuition Receipts; and
1987-88	Data from subsequently dissolved districts pro-rated into the receiving districts.

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NEBRASKA STATE DEPARTMENT OF EDUCATION
State Aid History

Year	Foundation	Incentive	Equalization	Total
1989/90	$ 96,376,100	$ 3,649,748	$ 33,590,252	$ 133,616,100
1988/89	96,376,098	3,638,839	33,601,163	133,616,100
1987/88	87,360,409	3,602,555	31,620,750	122,583,714
		(2% reduction from 1986-87 appropriation)		
1986/87	89,157,582	3,598,240	32,349,540	125,105,362
		(1.5% reduction/Special Session-December, 1986)		
1986/87	90,515,325	3,598,240	32,896,960	127,010,525
1985/86	90,615,324	3,569,721	32,925,480	127,110,525
		(3% reduction/Special Session-November, 1985)		
1985/86	94,546,578	3,566,246	32,928,944	131,041,768
		(2% reduction from 84-85 appropriation)		
1984/85	96,476,100	3,497,557	33,742,443	133,716,100
1983/84	96,476,100	3,458,516	33,781,484	133,716,100
1982/83	96,476,100	3,490,414	33,749,586	133,716,100
		(2% reduction/Special Session-November, 1982)		
1982/83	98,445,000	3,490,414	34,509,586	136,445,000
1981/82	56,999,999	3,471,781	34,528,219	95,000,000
1980/81	57,000,000	3,616,358	34,383,642	95,000,000
1979/80	24,428,771	3,596,962	26,974,266	54,999,999
1978/79	21,501,597	3,545,751	29,952,650	54,999,999
1977/78	19,652,815	3,491,071	31,856,113	54,999,999
1976/77	22,314,899	3,380,703	29,304,391	54,999,999
1975/76	19,947,227	3,307,736	29,246,244	52,501,208
1974/75	22,609,055	3,201,371	29,188,587	54,999,013
1973/74	22,760,534	3,100,674	29,138,413	54,999,621
1972/73	12,871,313	2,959,267	19,169,418	34,999,998
1971/72	12,833,060	2,812,100	19,354,839	34,999,999
1970/71	12,714,729	2,632,515	19,652,755	34,999,999
1969/70	12,643,990	2,552,866	19,803,144	35,000,000
1968/69	8,865,090	2,344,075	13,790,602	24,999,767

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Appendix C. School Finance At A Glance

DISTRIBUTION OF VALUATION AND STUDENTS IN NEBRASKA PUBLIC SCHOOL DISTRICTS - 1987-88

CLASS OF DISTRICT	NUMBER OF CLASS 1-5 DISTRICTS	TOTAL VALUATION OF CLASS 1-5 DISTRICTS	TOTAL K-12 RESIDENT ENROLLMENT	AVERAGE VALUATION PER K-12 RESIDENT ENROLLEE	PERCENT OF TOTAL STATE K-12 RESIDENT ENROLLMENT	PERCENT OF TOTAL STATE CLASS 1-5 VALUATION
1 (NOT IN CLASS 6)	409	3,841,831,452	12,004	320,046	4.52	8.68
1 (IN CLASS 6)	181	2,547,546,764	11,917	213,774	4.49	5.76
CLASS 1 TOTALS	590	6,389,378,216	23,921	267,103	9.01	14.44
2	54	1,757,446,308	7,573	232,067	2.85	3.97
3	222	24,739,162,006	167,425	147,763	63.04	55.92
4	1	4,542,250,724	25,459	178,414	9.59	10.27
5	1	6,811,223,138	41,228	165,209	15.52	15.40
CLASS 2-5 TOTALS	278	37,850,082,176	241,685	156,609	90.99	85.56
STATE TOTALS	868	44,239,460,392	265,606	166,560	100.00	100.00

NOTE: THE RESIDENT ENROLLMENT FIGURE FOR THE CLASS "1 (NOT IN CLASS 6)" CATEGORY INCLUDES HIGH-SCHOOL STUDENTS FROM CLASS 1 DISTRICTS WHO ATTEND HIGH SCHOOL UNDER THE COUNTY NONRESIDENT HIGH SCHOOL TUITION FUND (3,588 STUDENTS).

THE RESIDENT ENROLLMENT FIGURE FOR THE CLASS "1 (IN CLASS 6)" CATEGORY INCLUDES STUDENTS FROM CLASS 1 DISTRICTS WHO ATTEND SECONDARY SCHOOL IN THE 23 CLASS 6 DISTRICTS ON A RESIDENT BASIS (4,005 STUDENTS).

DISTRIBUTION OF REVENUES AND EXPENDITURES IN NEBRASKA PUBLIC SCHOOL DISTRICTS - 1987-88

CLASS OF DISTRICT	NUMBER OF DISTRICTS	AVERAGE DAILY MEMBERSHIP	TOTAL REVENUES	REVENUE PER STUDENT IN AVERAGE DAILY MEMBERSHIP	TOTAL ANNUAL COST	ANNUAL COST PER STUDENT IN AVERAGE DAILY MEMBERSHIP
1	590	15,802.40	50,565,976.66	3,199.89	46,822,565.62	2,963.00
2	54	7,835.95	39,389,794.58	5,026.81	38,314,120.89	4,889.53
3	222	170,318.93	639,421,237.17	3,754.26	587,109,257.50	3,447.12
4	1	25,533.05	88,032,352.84	3,447.78	96,515,554.47	3,780.02
5	1	40,323.87	157,273,960.45	3,900.27	144,468,738.81	3,582.71
CLASS 2-5 TOTALS	278	244,011.80	924,117,345.04	3,787.18	866,407,671.67	3,550.68
6	23	4,403.55	22,940,346.68	5,209.51	23,114,199.81	5,248.99
STATE TOTALS	891	264,217.75	997,623,668.38	3,775.76	936,344,437.10	3,543.84

NOTE: DATA IS FROM THE ANNUAL FINANCIAL REPORTS OF SCHOOL DISTRICTS. "TOTAL REVENUES" ARE TAKEN FROM LINE 70 OF THE REPORTS, "TOTAL ANNUAL COST" IS TAKEN FROM LINE 472, AND "AVERAGE DAILY MEMBERSHIP" IS TAKEN FROM LINE 468.

1987-88 REVENUES TO LOCAL SCHOOL DISTRICTS BY TYPE AND PERCENTAGE OF TOTAL

	REVENUES	PERCENTAGE THIS CATEGORY IS OF ALL REVENUES
LOCAL TAXES (PROPERTY AND PUBLIC POWER DISTRICT SALES)	598,485,095.40	59.99
LOCAL TUITION RECEIVED	7,426,196.45	0.74
TRANSPORTATION FROM OTHER DISTRICTS AND INDIVIDUALS	170,573.01	0.02
INTEREST EARNED ON LOCAL REVENUE RECEIPTS	9,918,446.03	0.99
FINES AND LICENSES (LOCAL AND COUNTY)	11,469,702.62	1.15
OTHER MISCELLANEOUS LOCAL, COUNTY, AND ESU RECEIPTS	3,988,907.96	0.40
NONRESIDENT HIGH SCHOOL TUITION	31,585,548.10	3.17
HOMESTEAD EXEMPTION	15,713,345.02	1.58
PRORATE MOTOR VEHICLE	2,189,769.05	0.22
STATE AID	120,861,959.76	12.11
SPECIAL EDUCATION (FROM STATE)	57,160,527.08	5.73
PAYMENTS FOR WARDS OF THE STATE	2,223,009.93	0.22
STATE APPORTIONMENT	14,136,798.57	1.42
IN-LIEU-OF SCHOOL LAND TAX	4,986,844.02	0.50
INSURANCE PREMIUM TAX	10,391,968.68	1.04
OTHER MISCELLANEOUS STATE RECEIPTS	1,428,399.31	0.14
NONCATEGORICAL FEDERAL (IMPACT AID & JOHNSON-O'MALLEY)	19,322,863.24	1.94
TOTAL NON-REVENUE RECEIPTS	38,781,897.85	3.89
TOTAL CATEGORICAL FEDERAL RECEIPTS	47,381,816.30	4.75
GRAND TOTAL OF ALL REVENUE	997,623,668.38	100.00

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PAYMENT YEAR 1988-89 STATE AID INFORMATION TOTAL AID = 133,616,100.07

FOUNDATION = 96,376,098.00 INCENTIVE = 3,644,514.00 EQUALIZATION = 33,595,488.07

CLASS OF DISTRICT	TOTAL IN CLASS	NUMBER RECEIVING FOUNDATION	FOUNDATION RECEIVED	NUMBER RECEIVING INCENTIVE	INCENTIVE RECEIVED	NUMBER RECEIVING EQUALIZATION	EQUALIZATION RECEIVED	NUMBER RECEIVING ANY AID	TOTAL AID RECEIVED
COUNTY *	93	64	1,689,411.03	0	.00	0	.00	64	1,689,411.03
CLASS 1	590	588	5,244,606.84	542	211,543.50	134	1,694,834.51	588	7,150,984.85
CLASS 2	54	54	2,780,873.07	54	155,634.50	19	751,870.23	54	3,688,377.80
CLASS 3	222	222	60,865,462.10	222	2,294,092.50	124	28,184,316.50	222	91,343,871.10
CLASS 4	1	1	9,194,212.82	1	328,093.50	0	.00	1	9,522,306.32
CLASS 5	1	1	14,803,027.37	1	574,225.00	1	2,626,404.12	1	18,003,656.49
CLASS 6	23	23	1,798,504.77	23	80,925.00	9	338,062.71	23	2,217,492.48
STATE TOTALS	984	953	96,376,098.00	843	3,644,514.00	287	33,595,488.07	953	133,616,100.07

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NUMBER OF RESIDENT STUDENTS IN DISTRICTS RECEIVING FOUNDATION AID = 266,240

NUMBER OF RESIDENT STUDENTS IN DISTRICTS RECEIVING INCENTIVE AID = 261,934

NUMBER OF RESIDENT STUDENTS IN DISTRICTS RECEIVING EQUALIZATION AID = 178,306

NUMBER OF RESIDENT STUDENTS IN DISTRICTS RECEIVING ANY AID = 266,240

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* COUNTY NONRESIDENT HIGH SCHOOL TUITION FUND

Appendix D. Estimated Revenue And Non-Revenue Receipts, 1988-89

TABLE 9.--ESTIMATED REVENUE AND NONREVENUE RECEIPTS, 1988-89

REGION AND STATE	REVENUE RECEIPTS BY SOURCE (IN THOUSANDS) FEDERAL	STATE	LOCAL AND OTHER	TOTAL	PERCENT OF REVENUE RECEIPTS BY SOURCE FEDERAL	STATE	LOCAL AND OTHER	NONREVENUE RECEIPTS (IN THOUSANDS)	TOTAL RECEIPTS (COLS. 5 AND 9) (IN THOUSANDS)
1	2	3	4	5	6	7	8	9	10
50 STATES AND D.C.	$11,645,928	$93,018,478	$80,457,572	$185,121,978	6.3	50.2	43.5	$7,853,657	$192,975,635
NEW ENGLAND	501,960	4,671,060	5,602,022	10,775,042	4.7	43.4	52.0	169,511	10,944,553
CONNECTICUT	133,400	1,513,500	1,667,800	3,314,700	4.0	45.7	50.3	1,200	3,315,900
MAINE	68,000	532,101	394,329	994,430	6.8	53.5	39.7	30,000	1,024,430
MASSACHUSETTS	219,466*	2,019,983*	2,239,448*	4,478,897*	4.9*	45.1*	50.0*	3,803*	4,482,700*
NEW HAMPSHIRE	21,303	50,909	651,843	724,055	2.9	7.0	90.0	121,993	846,048
RHODE ISLAND	30,791*	346,567	383,602	760,960	4.0	45.5	50.4	15	760,975
VERMONT	29,000	208,000	265,000	502,000	5.8	41.4	52.8	12,500	514,500
MIDEAST	1,931,209	17,684,836	20,488,210	40,054,255	4.8	44.2	51.0	1,791,816	41,846,071
DELAWARE	41,853	355,361	124,830	522,044	8.0	68.1	23.9	14,100	536,144
DIST. OF COLUMBIA	53,101	...	452,403	505,504	10.5	...	89.5	0	505,504
MARYLAND	195,235	1,468,505	2,066,447	3,730,207	5.2	39.4	55.4	22,716	3,752,923
NEW JERSEY	321,000	3,509,700	4,222,500	8,053,200	4.0	43.6	52.4	105,000	8,158,200
NEW YORK	900,000	7,987,470	8,984,530	17,872,000	5.0	44.7	50.3	650,000	18,522,000
PENNSYLVANIA	420,000	4,363,800	4,587,500	9,371,300	4.5	46.6	49.0	1,000,000	10,371,300
SOUTHEAST	3,032,190	21,024,152	13,724,937	37,781,279	8.0	55.6	36.3	1,766,686	39,547,915
ALABAMA	250,000	1,520,300	360,000	2,130,300	11.7	71.4	16.9	110,000	2,240,300
ARKANSAS	126,509	826,551	405,360	1,358,420	9.3	60.8	29.8	23,644	1,382,064
FLORIDA	532,466	4,576,052	3,403,348	8,511,866	6.3	53.8	40.0	627,603	9,139,469
GEORGIA	321,024*	2,699,807*	1,501,122*	4,521,453*	7.1*	59.7*	33.2*	9,060*	4,530,513*
KENTUCKY	220,800	1,552,310	446,480	2,219,590	9.9	69.9	20.1	205,030	2,424,620
LOUISIANA	300,090*	1,368,300*	814,520*	2,482,910*	12.1*	55.1*	32.8*	210,610*	2,693,520*
MISSISSIPPI	223,914*	810,177*	454,311*	1,488,402*	15.0*	54.4*	30.5*	110,215*	1,598,617*
NORTH CAROLINA	289,390	2,679,800	1,246,300	4,215,490	6.9	63.6	29.6	25,900	4,241,390
SOUTH CAROLINA	183,500	1,248,400	860,000	2,291,900	8.0	54.5	37.5	159,000	2,450,900
TENNESSEE	254,007	1,315,536	1,076,506	2,646,049	9.6	49.7	40.7	193,699	2,839,748
VIRGINIA	215,990	1,588,169	2,786,924	4,591,083	4.7	34.6	60.7	89,475	4,680,558
WEST VIRGINIA	114,500	839,250	370,066	1,323,816	8.6	63.4	28.0	2,400	1,326,216
GREAT LAKES	1,625,827	12,837,423	15,615,345	30,078,595	5.4	42.7	51.9	1,372,858	31,451,453
ILLINOIS	665,322	2,990,110	4,500,000	8,155,432	8.2	36.7	55.2	578,400*	8,733,832
INDIANA	155,620*	2,328,429*	1,355,529*	3,839,578*	4.1*	60.6*	35.3*	79,393*	3,918,971*
MICHIGAN	285,784*	2,641,572*	4,354,629*	7,281,985*	3.9*	36.3*	59.8*	148,086*	7,430,071*
OHIO	353,801	3,369,912	3,326,287	7,050,000	5.0	47.8	47.2	475,731	7,525,731
WISCONSIN	169,300	1,507,400	2,078,900	3,751,600	4.4	40.2	55.4	91,248	3,842,848
PLAINS	673,979	5,677,395	6,327,359	12,678,733	5.3	44.8	49.9	403,003	13,081,736
IOWA	111,141	911,470	952,529	1,975,140	5.6	46.1	48.2	78,704	2,053,844
KANSAS	101,666	822,566	980,143	1,904,375	5.3	43.2	51.5	43,500	1,947,875
MINNESOTA	152,200	1,965,500	1,385,200	3,502,900	4.3	56.1	39.5	110,000	3,612,900
MISSOURI	186,000	1,380,539	1,835,507	3,402,046	5.5	40.6	54.0	110,000	3,512,046
NEBRASKA	52,680*	249,105*	713,012*	1,014,797*	5.2*	24.5*	70.3*	26,368*	1,041,165*
NORTH DAKOTA	31,241*	223,616*	180,000	434,857	7.2	51.4	41.4	15,000	449,857
SOUTH DAKOTA	39,051*	124,599*	280,968*	444,618*	8.8*	28.0*	63.2*	19,431*	464,049*
SOUTHWEST	1,455,711	8,889,438	8,131,306	18,476,455	7.9	48.1	44.0	1,876,283	20,352,738
ARIZONA	91,533*	1,185,786*	1,060,724*	2,338,043*	3.9*	50.7*	45.4*	369,000*	2,707,043*
NEW MEXICO	138,600*	828,325*	129,186*	1,091,111*	12.2*	75.9*	11.8*	37,939*	1,129,050*
OKLAHOMA	170,000	1,130,000	510,000	1,810,000	9.4	62.4	28.2	130,000	1,940,000
TEXAS	1,060,578	5,745,327	6,431,396	13,237,301	8.0	43.4	48.6	1,339,344	14,576,645
ROCKY MOUNTAINS	331,851	2,732,932	2,721,987	5,786,770	5.7	47.2	47.0	87,970	5,874,740
COLORADO	127,543*	1,030,750*	1,515,838*	2,674,131*	4.8*	38.5*	56.7*	28,562*	2,702,693*
IDAHO	46,000	395,000	215,600	656,600	7.0	60.2	32.8	12,000	668,600
MONTANA	59,236*	345,832*	306,854*	711,922*	8.3*	48.6*	43.1*	14,887*	726,809*
UTAH	74,072	676,350	443,695	1,194,117	6.2	56.6	37.2	12,521	1,206,638
WYOMING	25,000	285,000	240,000	550,000	4.5	51.8	43.6	20,000	570,000
FAR WEST	2,093,201	19,501,242	7,896,406	29,490,849	7.1	66.1	26.8	385,580	29,876,429
ALASKA	61,795*	440,765*	190,383*	692,943*	8.9*	63.6*	27.5*	85,700*	778,643*
CALIFORNIA	1,592,607	14,897,849	5,060,190	21,550,646	7.4	69.1	23.5	135,210	21,685,856
HAWAII	57,600	665,700	900	724,200	8.0	91.9	0.1	0	724,200
NEVADA	30,662	283,025	405,978	719,665	4.3	39.3	56.4	3,962	723,627
OREGON	137,400	584,700	1,471,800	2,193,900	6.3	26.7	67.1	31,500	2,225,400
WASHINGTON	213,137	2,629,203	767,155	3,609,495	5.9	72.8	21.3	129,208	3,738,703

Source: Data Search
Estimates of School Statistics (1988-89)
National Education Association

*NEA Estimates

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Appendix E. Proposed Average Daily Membership Tiers

MODEL "D" - NEBRASKA SCHOOL FINANCING REVIEW COMMISSION "TIERS" BASED ON 1987-88
SCHOOL DISTRICT GENERAL FUND OPERATING EXPENDITURES* PER STUDENT IN AVERAGE DAILY MEMBERSHIP (ADM)

GRADES 1-6 TIER	TIER RANGE (BASED ON GRADES 1-6 ADM)	GRADES 1-6 TIER MIDPOINT	NUMBER OF DISTRICTS	GRADES 1-6 GENERAL FUND OPERATING EXPENDITURES	ADM GRADES 1-6	GENERAL FUND OPERATING EXPENDITURES PER ADM
1	.01 - 101.00	50.50	631	49,249,826.70	14,122.50	3,487.33
2	101.01 - 185.00	143.00	107	46,606,520.41	14,226.63	3,276.01
3	185.01 - 375.00	280.00	55	42,264,452.00	14,114.34	2,994.43
4	375.01 - 1,000.00	687.50	24	39,009,037.38	13,980.44	2,790.26
5	1,000.01 - 1,900.00	1,450.00	10	37,632,098.23	14,310.40	2,629.70
6	1,900.01 - 15,000.00	8,450.00	7	96,371,418.62	33,916.02	2,841.47
7	15,000.01 +	19,501.26	1	63,089,594.56	19,501.26	3,235.15
STATE TOTALS			835	374,222,947.90	124,171.59	3,013.76

GRADES 9-12 TIER	TIER RANGE (BASED ON GRADES 9-12 ADM)	GRADES 9-12 TIER MIDPOINT	NUMBER OF DISTRICTS	GRADES 9-12 GENERAL FUND OPERATING EXPENDITURES	ADM GRADES 9-12	GENERAL FUND OPERATING EXPENDITURES PER ADM
1	.01 - 50.00	25.00	48	12,670,823.63	1,875.70	6,755.25
2	50.01 - 75.00	62.50	66	22,879,041.96	4,216.80	5,425.69
3	75.01 - 100.00	87.50	49	21,287,465.01	4,244.16	5,015.71
4	100.01 - 150.00	125.00	42	22,877,053.70	5,219.30	4,383.17
5	150.01 - 250.00	200.00	44	36,020,038.30	8,363.19	4,306.97
6	250.01 - 500.00	375.00	30	41,716,836.09	10,384.45	4,017.24
7	500.01 - 1,000.00	750.00	10	25,565,884.96	7,212.42	3,544.70
8	1,000.01 - 10,000.00	5,500.00	11	102,730,177.41	25,523.20	4,024.97
9	10,000.01 +	11,078.45	1	50,176,700.71	11,078.45	4,529.22
STATE TOTALS			301	335,924,021.77	78,117.67	4,300.23

* "GENERAL FUND OPERATING EXPENDITURES" = TOTAL GENERAL FUND EXPENDITURES MINUS TOTAL TUITION PAID, ADULT EDUCATION, SUMMER SCHOOL, SCHOOL LUNCH PASS-THRU, TRANSFERS FROM OTHER FUNDS INTO THE GENERAL FUND, COMMUNITY SERVICES, AND THE REDEMPTION OF PRINCIPAL PORTION OF GENERAL FUND DEBT SERVICE.

NDE:MIS 12/12/89

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Appendix F. Statistical Equity Analysis Of The Current System

MEMORANDUM

To: The School Finance Review Commission

From: John Augenblick, Augenblick, Van de Water & Associates

Date: December 28, 1989

Re: The Equity of Nebraska's School Finance System

In October, Sen. Withem asked me to evaluate the equity of Nebraska's school finance system. I have now had a chance to review both the current school aid structure and the results it produces in terms of spending levels and tax rates across the state's school districts. While the level of equity produced by the system is somewhat better than anticipated, primarily because the variation in per pupil property wealth (over which the state has no control) is relatively low, there is plenty of room for improvement. The recommendations being made by the Commission are very important in order to improve the sensitivity of state aid both to the varying needs of school districts, caused primarily by the fiscal impact of operational scale (enrollment level), and the varying wealth (in terms of both property and income) of school districts in Nebraska.

The purpose of this memorandum is to summarize my findings and conclusions briefly. I think it is important to begin by placing Nebraska in a national context. In 1987-88, public schools in Nebraska spent about $600 less per pupil than the national average. The state ranked 33rd (from the top) among all states in terms of per pupil spending, a slight decrease in

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from 1982-83 when the state ranked 32nd, but a dramatic drop from 1977-78 when the state ranked 20th and had per pupil spending at about the national average.

This relative loss in spending level can be attributed to the fact that while per pupil spending has been increasing at a rate above inflation, that rate has been far below the national average increase in spending. Between 1977-78 and 1982-83, per pupil spending in Nebraska grew by 1.9 percent more than inflation, far below the national average rate, which was 10.4 percent above inflation; between 1982-83 and 1987-88, per pupil spending increased 10.2 percent faster than inflation in Nebraska while the national average increased at a rate 17.2 percent over inflation. This pattern of decline also affected teachers' salaries. In 1987-88, the average teacher salary in Nebraska was about $4,800 behind the national average and ranked 42nd among the 50 states (a decline from rankings of 38th in 1977-78 and 40th in 1982-83).

Nebraska relies very heavily on local taxes, a large proportion of which are derived from property taxes. In 1987, Nebraska generated $753 per capita in state taxes, about $250 less than the national average, while producing $704 in local taxes, about $54 above the national average. Relative to income, Nebraska's state tax burden was very low; in 1987, state taxes generated $5.48 per $100 of personal income, about 22 percent less than the national average (Nebraska ranked 46th among all states in state taxes per $100 of personal income).

In terms of local taxes, however, Nebraska collected $5.12 per $100 of personal income, about 15 percent above the national average (the state ranked 9th from the top on this measure). In Nebraska, property taxes represent 43

percent of all state and local taxes, compared to a national average of about 30 percent. Finally, since 1978, both state and local taxes have declined relative to income.

The current school finance system does little to promote equity among school districts. First, state aid provides a relatively low share of all school revenue. At a level under 30 percent of all revenue, state aid in Nebraska is well below the national average of about 50 percent. Among the 50 states, only in New Hampshire does state aid provide a significantly smaller share of school revenue than in Nebraska. Second, the majority of state support is distributed without any recognition for either the needs of school districts, which vary significantly due to such uncontrollable factors as district size, or differences in their fiscal capacities. Foundation revenue provides a "flat" amount, which differ by grade level, regardless of the size of a district or its property wealth. Equalization aid is sensitive to both size (sparsity) and wealth but provides less than five percent of all school district revenues. The combination of a low level of support and a lack of targeting of aid results in an inefficient use of state funds.

An evaluation of school finance equity requires an examination of the disparity in certain school finance variables, such as the wealth of districts, their spending levels, and their tax rates, and the relationships that exist among those variables. Of primary interest is the variation in the wealth of districts. This is the case because, given that property wealth would be the chief source of funding for schools if state aid were not provided, either district spending would reflect the availability of property wealth or tax rates would be inversely proportion to that wealth in order for districts to have similar spending levels.

In Nebraska, there is significant variation in the per pupil property wealth of school districts. In fact, for districts with any resident enrollment, property wealth ranges form over $4 million per pupil to under $8,000 per pupil. The following table indicates the distribution of districts in terms of per pupil property wealth:

Range of Property Wealth Per Pupil	Proportion of All Districts
More than $400,000	23.8%
$300,000 - $399,999	13.0%
$200,000 - $299,999	28.4%
$100,000 - $199,999	28.2%
Less than $100,000	6.6%

A single statistic, the coefficient of variation (c.v.), can be used to indicate the amount of "spread" in the system. The coefficient of variation is simply the standard deviation divided by the mean. The c.v. is a valuable indicator of dispersion because it: (1) uses data for all school districts, not just the extreme cases; (2) emphasizes outliers because in the calculation of the standard deviation, differences between each case and the mean are squared; (3) is normed by the mean for comparison over time and to other states; and (4) it is unaffected by year to year changes caused solely by factors such as inflation.

When I calculate the c.v., I "weight" it to reflect the different enrollments of each school district. That is, each district does not have the same impact on the result; rather, each district affects the result in proportion to its enrollment. This is important because I am interested in

the impact of state policy on pupils, not school districts, which are only convenient agencies through which the state fulfills its legal obligation to provide education services to all pupils no matter where they live in the state. The coefficient of variation can be as low as zero, which indicates the absolute equality of all districts. The higher the c.v. is, the greater the disparity it indicates.

The coefficient of variation for per pupil property wealth is .451, which means that about two-thirds of all pupils are enrolled in districts where the property wealth per pupil ranges from 45.1 percent below the mean to 45.1 percent above the mean. Given a mean property wealth of about $163,000 per pupil, this indicates that two-thirds of Nebraska's pupils reside in school districts with wealth that ranges from about $89,000 per pupil to about $236,000 per pupil.

The greater the variation in property wealth, the harder the school finance system needs to work to "neutralize" the impact of wealth on the spending and tax rate decisions of school districts. In my experience, it is not unusual for the c.v. of per pupil property wealth to be .700 or higher. Given the large number of school districts in Nebraska, I expected the variation to be greater. Fortunately, and due only to chance rather than state action, the variation in property wealth, while high in an absolute sense, is comparatively low.

One of the most critical concerns in evaluating the equity of a school finance system is the extent of the variation in per pupil spending. This is typically the focus of plaintiffs in school finance litigation under the theory that variations in spending reflect differences in educational opportunities assured in equal protection or education clauses contained in

state constitutions. In Nebraska, there is considerable variation in the per pupil spending of school districts, as shown in the following table:

Range of Per Pupil Spending	Proportion of All Districts
More than $5,000	14.8%
$4,000 - $4,999	19.2%
$3,000 - $3,999	31.7%
$2,000 - $2,999	28.4%
Less than $2,000	5.9%

The highest spending district in the state spent over $39,000 per pupil while the lowest spending district spent under $1,200 per pupil. Excluding transportation expenditures, which can differ substantially across districts for legitimate reasons, average spending is about $3,400 while the coefficient of variation for per pupil spending, excluding transportation, is .220. This means that about two-thirds of all pupils were enrolled in districts spending between about $2,600 and $4,100. While this variation is not outrageously high, particularly given the fact that the size of districts may explain some of this variation, it is certainly high enough to justify close examination of spending differences. It should also be noted that the c.v. of per pupil spending for Kentucky, a state where the entire system of education was declared unconstitutional last June, was .200, slightly lower than that found in Nebraska.

Also of importance is the relationship between the per pupil spending and per pupil wealth of districts. This is the case because a strong positive relationship indicates a lack of "fiscal neutrality", which has served as the

basis for declaring school finance systems unconstitutional since the Serrano case in California in the early 1970's. I use the correlation coefficient to measure the strength of a relationship between two variables. The correlation coefficient ranges from -1.00 to +1.00; a positive relationship indicates that as one variable increases the other does also, while a negative relationship indicates that as one variable increases the other tends to decrease. In fact, the correlation between per pupil spending and per pupil wealth is +.57 in Nebraska, indicating a moderate, positive relationship. The combination of a moderate level of disparity in per pupil spending and a positive relationship between spending and wealth makes Nebraska vulnerable to litigation, particularly if education is considered to be a "fundamental interest" under the state's constitution.

As I showed previously, the structure of the state aid system does not help to overcome the inequity that results from the disparity in property wealth. In fact, the disparity in state aid per pupil is very low, as shown in the following table:

Range of Per Pupil State Aid	Proportion of All Districts
More than $700	6.4%
$600 - $699	4.8%
$500 - $599	6.1%
$400 - $499	17.8%
$300 - $399	58.6%
Less than $300	6.3%

Even though the range in property wealth per pupil is not extremely high in Nebraska, the range in state aid per pupil is very low, with most districts receiving between $300 and $500 per pupil. This means that, under the current system being used to distribute state support, the limited funds provided by the state do little to deal with differences in the wealth of districts. As I have already pointed out, state aid is not currently very sensitive to district needs, particularly those related to size.

Another problem with the current system is that it permits a wide variation in the property tax rates of school districts. This not only creates equity problems for pupils, since districts with high wealth and high tax rates will have high spending levels, it creates equity problems for taxpayers. In a state that relies as heavily as Nebraska does on property taxes, this situation is inappropriate. The following table illustrates the disparity in the tax rates of school districts:

Range of Property Tax Rates	Proportion of All Districts
More than $2.00	10.3%
$1.75 - $1.99	11.7%
$1.50 - $1.74	18.0%
$1.25 - $1.49	23.9%
$1.00 - $1.24	22.6%
Less than $1.00	13.5%

Tax rates range from less than $.45 to over $3.40 across all districts. The coefficient of variation for tax rate is .167 for the general levy and .178 for the total levy, indicating that two-thirds of all pupils are enrolled

in districts with tax rates between about $1.45 and $2.00. Of equal concern is the fact that tax rates are negatively correlated with property wealth (correlation coefficient is -.53 for total tax rate), indicating that wealthy districts tend to have lower tax rates than their less wealthy peers. Finally, the relationship between tax rates and per pupil spending levels is slightly negative (correlation coefficient is -.19 for total tax rate).

In some states, tax rate variation is considered to be a reasonable cause for per pupil spending differences, under the theory that a variation in tax rates reflects local control and that spending differences caused by local control are acceptable. Even if this theory were accepted in Nebraska, there would need to be a strong, positive relationship between tax rates and spending levels, not the negative relationship that actually exists.

While my evaluation was done quickly, using data for only one year, it reveals that the there are a variety of inequities in the Nebraska's school finance system and that the way state aid is distributed does little to rectify them. In fact, the system only looks as good as it does because of the relatively low disparity in property wealth, over which the state has no control. If the disparity in property wealth were to increase, the method of allocating state aid would not be very responsive, which would likely lead to greater inequities in per pupil spending or property tax rates.

I am grateful to Tim Kemper of the Department of Education for his help in organizing the data used in this analysis and producing the basic statistics I requested in a timely manner. Without his help, it would not have been possible for me to fulfill the request of the Commission, particularly given the large number of districts in the state and the way in which they are organized.

I hope this information is useful to you. I support the need to change the approach used to distribute state aid and encourage the Commission to make the new system more sensitive to the variations in both the needs and fiscal capacities of school districts.

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Appendix G. Effects Of Additional Aid On Total Property Taxes Levied

EFFECTS OF ADDITIONAL AID ON TOTAL PROPERTY TAXES LEVIED

State Aid as % of school spending	45.0%
Growth in property valuations	4.0%
Growth in taxes levied	6.5%
Growth in taxes levied with cap *	5.5%

Tax Year	Total Valuation	CURRENT TREND — Taxes Levied	% Chge	Avg Levy	WITH SCHOOL FINANCE PROPOSALS / 1884 — Increased Aid	Taxes Levied	Avg Levy	% reduction **
1970	15,358,786,223	352,520,994	8.33%	2.295%	0	352,520,994	2.295%	na
1971	15,822,576,380	390,787,447	10.86%	2.470%	0	390,787,447	2.470%	na
1972	16,375,816,726	410,464,626	5.04%	2.507%	0	410,464,626	2.507%	na
1973	17,363,662,554	415,893,062	1.32%	2.395%	0	415,893,062	2.395%	na
1974	18,580,766,406	453,597,038	9.07%	2.441%	0	453,597,038	2.441%	na
1975	19,280,640,037	527,417,745	16.27%	2.735%	0	527,417,745	2.735%	na
1976	20,050,797,594	597,045,719	13.20%	2.978%	0	597,045,719	2.978%	na
1977	21,793,525,506	640,633,655	7.30%	2.940%	0	640,633,655	2.940%	na
1978	21,753,300,431	631,182,815	(1.48%)	2.902%	0	631,182,815	2.902%	na
1979	34,230,878,709	685,227,648	8.56%	2.002%	0	685,227,648	2.002%	na
1980	36,204,907,463	710,984,868	3.76%	1.964%	0	710,984,868	1.964%	na
1981	37,323,254,040	775,250,227	9.04%	2.077%	0	775,250,227	2.077%	na
1982	38,553,689,126	821,983,034	6.03%	2.132%	0	821,983,034	2.132%	na
1983	41,035,051,584	895,512,735	8.95%	2.182%	0	895,512,735	2.182%	na
1984	41,632,906,878	950,426,265	6.13%	2.283%	0	950,426,265	2.283%	na
1985	44,606,914,842	1,016,558,636	6.96%	2.279%	0	1,016,558,636	2.279%	na
1986	43,847,711,624	1,060,100,433	4.28%	2.418%	0	1,060,100,433	2.418%	na
1987	44,386,604,162	1,100,975,102	3.86%	2.480%	0	1,100,975,102	2.480%	na
1988	44,697,049,210	1,167,482,844	6.04%	2.612%	0	1,167,482,844	2.612%	na
Projected ***								
1989	49,900,000,000	1,307,580,785	12.00%	2.620%	(113,000,000)	1,194,580,785	2.394%	(8.6%)
Projected								
1990	51,896,000,000	1,392,573,536	6.50%	2.683%	(211,347,429)	1,168,150,300	2.251%	(16.1%)
1991	53,971,840,000	1,483,090,816	6.50%	2.748%	(227,992,864)	1,227,377,240	2.274%	(17.2%)
1992	56,130,713,600	1,579,491,719	6.50%	2.814%	(245,285,483)	1,290,129,977	2.298%	(18.3%)
1993	58,375,942,144	1,682,158,681	6.50%	2.882%	(263,186,644)	1,356,676,665	2.324%	(19.3%)
1994	60,710,979,830	1,791,498,995	6.50%	2.951%	(281,765,668)	1,427,190,124	2.351%	(20.3%)
1995	63,139,419,023	1,907,946,430	6.50%	3.022%	(301,038,396)	1,501,909,964	2.379%	(21.3%)
1996	65,664,995,784	2,031,962,948	6.50%	3.094%	(321,020,002)	1,581,090,518	2.408%	(22.2%)
1997	68,291,595,615	2,164,040,540	6.50%	3.169%	(341,724,841)	1,665,001,758	2.438%	(23.1%)
1998	71,023,259,440	2,304,703,175	6.50%	3.245%	(363,166,275)	1,753,930,287	2.470%	(23.9%)
1999	73,864,189,817	2,454,508,881	6.50%	3.323%	(385,356,493)	1,848,180,380	2.502%	(24.7%)
2000	76,818,757,410	2,614,051,958	6.50%	3.403%	(408,305,299)	1,948,075,101	2.536%	(25.5%)

* Assuming a 5% growth in property taxes for schools due to the impact of the cap, the TOTAL property taxes levied should be reduced from a 6.5% average growth to 5.5% average growth.

** This column reflects the percent reduction in property taxes with the School Finance proposal (increased aid and 5.5% property tax growth) compared to the current trend (6.5% growth in property taxes)

*** 1989 figures include the following assumptions:
(1) Preliminary figures from the Dept of Revenue on valuations
(2) Assumed 12% increase in property taxes levied.
(3) $113 million reduction in property taxes levied due to 1884

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END

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March 29, 1991